Employment status in SMEs

A research study for HM Revenue and Customs

HMRC report 455

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Contents

Tables

Figures

Glossary

CATI
Computer-assisted telephone interviewing. A common telephone survey technique where trained interviewers read and complete a computerised script.

Employment status
The official classification of an individual based on the work that they do. There are three main types of employment status: employee, worker and self-employed. An individual's employment status helps to determine their employment rights, their employer's responsibilities, and how the individual pays tax, National Insurance and some entitlements. For tax purposes, individuals are considered to be either employed or self-employed.

ESI tool
The Employment Status Indicator tool. An online tool, developed by HMRC, to enable businesses and individuals to check the employment status of an individual or group of workers for tax purposes.

HMRC
Her Majesty's Revenue and Customs, the UK's tax, payments, and customs authority. A non-ministerial department of the UK Government.

IDBR
The Inter-Departmental Business Register. A comprehensive list of UK businesses used by government for statistical purposes and held by the Office for National Statistics (ONS). It is fully compliant with the European Union regulation on harmonisation of business registers for statistical purposes.

Medium company
A company that has 50-249 employees. This was the definition used in this research.

Micro company
A company that has nine employees or fewer. For the purpose of this research, micro companies with zero employees are excluded.

NatCen
The National Centre for Social Research. An independent, not for profit social research company.

PAYE
Pay As You Earn. A status of employment where the employer deducts income tax and national insurance contributions from an individual's wages before payment of wages.

Self-employed
A person is self-employed if they run their business for themselves and take responsibility for its success or failure. Self-employed workers are not paid through PAYE, and they do not have the employment rights and responsibilities of employees.

SIC 2007
The current Standard Industrial Classification (SIC). It is used in classifying business establishments and other statistical units by the type of economic activity in which they are engaged.

Small company

A company that has 10-49 employees. This definition was used in this research.

SME
Small and Medium sized Enterprises. The usual definition of small and medium sized enterprises (SMEs) is any business with fewer than 250 employees. However, as this project explores SME employers, for the purpose of this research all businesses with zero employees were excluded. Therefore, in this report 'SME' should be interpreted as meaning 'SME employer'.

SOC
The Standard Occupational Classification. It is a common classification of occupational information for the UK.

Executive summary

This report presents the findings from research conducted into Employment Status for HM Revenue and Customs (HMRC). The research was designed to provide robust evidence on the nature of employment in SMEs; understand how SMEs determine the employment status of their workers; explore awareness and use of the Employment Status Indicator (ESI) tool; and consider any ways in which HMRC can help SMEs classify the work status of their staff correctly.

To achieve this, a mixed method approach was adopted. The approach consisted of a CATI (telephone) survey of 1,722 SMEs, selected and interviewed using a stratified random probability design, and a series of 33 in-depth interviews with SMEs, identified as being potentially at risk of mis-categorising staff based on their responses to the quantitative survey.

This research was undertaken by the National Centre for Social Research (NatCen) on behalf of HMRC.

Profile of employment in SMEs

- More than four in five SMEs employ any staff on a PAYE basis (83%), regardless of whether they engage self-employed workers. Medium sized businesses are significantly more likely to employ PAYE staff than micro businesses (100% compared to 89%).
- A quarter of SMEs engage self-employed workers (23%). This proportion does not vary significantly according to the size of a business.
- Just over one in ten SMEs take on individuals through agencies (12%). Medium sized businesses are significantly more likely to take on agency workers than micro businesses (56% compared to 11%).
- Two in three SMEs only engage PAYE staff (66%). Six per cent only engage self-employed workers, and 17% engage both PAYE and self-employed staff.
- SMEs engage self-employed workers for all different job roles, but most commonly for roles in the middle of the occupational hierarchy, such as 'skilled tradespeople'.
- One in five SMEs say that employment numbers are seasonal and vary throughout the year (22%).

Determining employment status

- Responsibility for determining employment status varies across SMEs. In micro businesses it is ordinarily the role of the business owner or managing director. In small businesses it is commonly the role of a company secretary or operations manager, and in medium sized companies it tends to be the responsibility of a specialist, such as a finance director or HR official.
- When determining the employment status of an individual, 71% of SMEs seek advice from an accountant, lawyer, or legal advisor.
- Half of SMEs use guidance on the HMRC or GOV.uk websites (49%) and 43% contact HMRC staff directly.
- Four per cent of SMEs give staff a choice over their employment status, with two per cent doing so regularly. This rises to 23% of businesses within the arts sector, and nine per cent in the construction industry.

- There are five main approaches to categorising employment status in SMEs:

- Only employing staff on PAYE terms. This is seen as the safest option, to ensure fair treatment of staff and minimise risk of investigation.
    - Offering PAYE terms by default but considering self-employment if requested or in exceptional circumstances;
    - Giving staff a choice. While considered more risky, this is often used when recruiting specialist roles;
    - Making decisions on a case by case basis. This approach involves consideration of the skills required for a role, the number and regularity of hours, and the duration of the employment;
    - Engaging staff on self-employed terms by default. This is less common and tends to be used in businesses that are unable to operate a PAYE system, or as a trial for high paid roles.
- As well as the nature of the role, such as the length and type of work, a number of factors are considered by SMEs when determining employment status, though these are not necessarily factors that HMRC requires them to take into account. These include:
    - Whether an individual has existing self-employed status;
    - Any risk to the business;
    - The administrative burden of operating a PAYE system;
    - The costs associated with PAYE, such as pensions, holiday pay and training; and
    - Historic or industry-standard practice.
- Virtually all SMEs are confident that they make the correct decisions when categorising the employment status of their workers (97%).
- A lack of confidence can stem from one or both of the following: uncertainty about the distinction between employment status categories, or observed ambiguities between categories in specific workforce roles.
- Just one per cent of SMEs say they experience difficulties when categorising staff. This is slightly higher in medium sized businesses (four per cent) and in certain sectors: Agriculture (eight per cent); the Arts (seven per cent); and Health/social work (six per cent).
- The difficulties SMEs describe range from experiencing uncertainty about employment status definitions to confronting more concrete situations such as when staff request an alternative classification; when self-employed staff carry out their work in the way employees typically do; and when HMRC has investigated a categorisation decision.

The Employment Status Indicator tool

- A quarter of SMEs are aware of the ESI tool (24%), with awareness significantly higher among medium sized businesses (38%).
- Five per cent of SMEs have used the ESI tool at some point and two per cent currently use it. Reflecting their higher awareness, medium sized businesses are significantly more likely to use the tool (18%).
- Businesses in the arts sector are also significantly more likely to use the ESI tool (19%), perhaps reflecting the greater freedom given to workers to choose their own employment status in that sector. (23% of arts sector SMEs give staff a choice over their employment status, compared to an average of four per cent.)
- The main reason SMEs use the ESI tool is to address any uncertainty over an individual's work status, particularly in complex cases.
- Those who do use the tool tend to be positive about it.
    - 94% say that it is easy to use;
    - 79% say that it makes it easier to make the right decision when classifying workers; and
    - 77% say that the questions are easy to understand.

- While SMEs tend to find the tool useful, it is not relied upon to definitively determine employment status and is often used in conjunction with other sources, such as professional advice and industry standard practice.
- Reflecting this, SMEs have varying levels of confidence in the outcome the tool produces. While 35% of users are very confident that the tool gives the correct decisions, 25% are only fairly confident and 10% are not confident.
- Uncertain results also reduce confidence in the tool, and 17% of users have experienced an uncertain result. Most who have this experience default to classifying individuals as PAYE workers.
- Despite this, the tool is generally seen as useful and 83% of users would recommend the tool to other businesses.
- Suggestions for improving the ESI tool include:
  - Making the link to the tool on the introduction page more obvious.
  - Avoiding complicated terminology and ensuring the tool is written in plain English. If terminology or jargon is required, ensure sufficient explanation of any terms.
  - Ensuring questions have answers that cover all eventual scenarios. Potentially route users based on their business type so they only answer questions relevant to them.
  - Providing more detailed information about why a status was given on the outcome page.

- Overall, SMEs tend to have a limited awareness of the information and resources available to them from the government. This suggests it would helpful for SMEs if HMRC increased awareness of the resources that are already available.

- SMEs would also value additional resources being made available. In particular, visual and interactive resources which reduce the amount of reading necessary, or provide a substitute for personal interaction, would be helpful. Examples could include a flow chart to work through an individual's employment status, videos, webinars and online training, and forums (online, or in person) that allow employers to discuss their experiences of categorising employment status.

Introduction

Background and objectives

An individual's employment status – whether they are considered to be an employee on a PAYE contract, a worker, or self-employed – helps to determine their employment rights, their employer's responsibilities, and how the individual pays tax and National Insurance.[1] Inaccuracies in employment status categorisation can therefore result in the collection of incorrect tax contributions.[2]

As there is no straightforward legal definition of being employed or self-employed[3] the line between whether an individual is an employee and subject to PAYE rules, or is self-employed, is not always clear-cut.

In 2015, the Office of Tax Simplification (OTS) identified difficulties faced by employers and individuals in determining employment status as a growing problem.[4] Indeed, HMRC estimates that several million pounds in tax revenue is lost due to inaccuracies in employment status categorisation.

To add to the problem, the OTS suggests that available guidance can lack clarity and that there is reluctance among employers to use available resources designed to assist them in determining employment status. Specifically, there is a perception that HMRC's online Employment Status Indicator (ESI) tool is biased towards generating an 'employed' status[5] and the use of case law means businesses lack certainty about the outcomes produced by the ESI.

The OTS has called for the need to overcome barriers to the use of available resources such as the ESI to encourage greater use.[6]

However, there is currently a gap in evidence focusing on employers who directly engage non–PAYE workers, particularly SMEs, and the issues they face in determining employment status.

This research, therefore, is intended to improve understanding of the issues faced by SMEs, and to understand how HMRC can improve available resources such as the ESI.

In light of this, this research has been designed to meet the following objectives:

- Provide robust quantitative and qualitative evidence on the nature of employment in SMEs.
- Explore how SMEs determine the employment status of their workers.
- Understand awareness and use of the ESI tool, and identify improvements to the way it works.

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[1] Gov.uk (2014) Employment status: employed or self-employed.
[2] Please note that, for tax purposes, individuals are considered to be either employed or self-employed. The classification 'worker' only impacts on employment rights.
[3] Low Incomes Tax Reforms Group (2016) Am I employed, self-employed, both, or neither?
[4] OTS (2015) Employment Status Report
[5] OTS (2015) Employment Status Report
[6] ibid

Methodology

To meet these objectives, NatCen designed a mixed-mode project, combining a random probability telephone survey with a series of in-depth interviews.

Quantitative survey

The quantitative element consisted of a computer assisted telephone interviewing (CATI) survey of 1,722 SMEs, sampled using a stratified random probability design.

The sample was drawn from the Inter-Departmental Business Register (IDBR). To ensure an optimum and efficient sample selection, and to enable sub-group analysis on key groups of interest, the sample was stratified and selection targets were set for each strata. Specifically, targets were set to ensure a proportionate allocation by Government Office Region and nation, with an equal allocation by SIC category. In addition, small and medium-sized businesses were over-sampled. Once the data had been collected, corrective weights were applied to ensure the results reflect the population of SMEs in the UK.

All selected businesses were sent an advance letter, jointly branded with HMRC and NatCen logos, outlining the purpose of the research and why they had been selected. The sample was issued in batches and each number called a minimum of six times during the fieldwork period until a final outcome was recorded and the desired number of interviews was completed.

In total, 4,960 telephone numbers were called and 1,722 interviews completed, giving an unadjusted response rate of 35%. Once ineligible numbers had been excluded (including incorrect telephone numbers and businesses that had since gone out of business), the adjusted response rate was 40%.

Fieldwork was conducted by telephone between 12 October and 4 November 2016.

Prior to the mainstage fieldwork, a pilot stage was developed. This consisted of a total of 52 interviews conducted between 13 and 23 September 2016. Because it was not possible to access the IDBR sample within the timescales for the pilot survey, the pilot sample was randomly selected by HMRC from its internal database of VAT registered businesses. Therefore, the pilot primarily aimed to test contact procedures, comprehension, and the length of the questionnaire, rather than response rates. Based on the findings of the pilot the questionnaire was refined for the mainstage.

Survey data have been weighted to the profile of SMEs according to region, SIC and employment bands.

Qualitative interviews

The key purpose of the qualitative interview was to explore issues covered in the quantitative survey in more depth. There were two particular areas of interest: understanding the reasons for potential mis-categorisation for SMEs that were directly engaging staff and exploring how HMRC could most effectively respond to these issues, including improvements to HMRC's Employment Status Indicator (ESI) online tool.

A total of 33 SMEs took part in an in-depth qualitative interview. They were chosen on the basis of selected survey responses, which indicated risk of mis-categorising staff. For example, if they said they had experienced difficulty categorising; were not

confident with their categorisations; offered staff a choice of status; or had taken out insurance against an HMRC investigation into employment status. The sample of SMEs was also selected to reflect a mix of staff types (PAYE only, self-employed only and both) sizes; years trading; and use / non-use of the ESI tool (further details of the sampling criteria can be found in the separate technical summary for this report).

Twenty-three interviews were conducted over the telephone and explored the decision making around categorising employment status; experience of challenging situations; and views of help and support around categorisation. These interviews lasted up to 45 minutes. Ten interviews were conducted face-to-face. These interviews lasted up to one hour and explored the themes described above, as well as user testing of the ESI tool. Fieldwork took place between October 2016 and January 2017. Participating SMEs received £50 from NatCen as a token of thanks for their time and contribution.

All qualitative interviews were audio-recorded using encrypted digital recorders and transcribed verbatim. The data was managed and analysed using the Framework approach, from which case and theme based analysis was conducted.

Interpreting the findings

Quantitative survey

This is a survey of SME employers. However, for shorthand these will be defined as SMEs throughout this report.

It is important to note that fieldwork took place mostly in October 2016. However, employment within SMEs can be seasonal. To test the impact of this, SMEs were asked whether their employment patterns are seasonal. Overall, 22 per cent of SMEs say that the number of people they engage varies throughout the year. Among SMEs which do experience seasonal variation in staffing levels, most said that at the time of interviewing staffing levels were about the same as normal (70 per cent). A quarter said that they had fewer staff than normal (23 per cent) and seven per cent had more staff than normal. Taking account of *all* respondents (not just those with seasonal variation in employment patterns), this equates to two per cent of SMEs with more staff than usual and five per cent with fewer than normal. As such, seasonality is unlikely to have had a notable impact on the research findings.

Each finding commented on in the report has been tested and found to be statistically significant, unless otherwise specified. A result is called statistically significant if it has been predicted as unlikely to have occurred by chance alone, according to a pre-determined threshold probability, which is known as the significance level. Significance tests have been undertaken at the 95% significance level. This means that we can be 95% confident that any significant result in this report is actually the case in the full population of registrants, and has not occurred by chance alone.

Where percentages do not sum to 100, this may be due to computer rounding, the exclusion of "don't know" categories, or multiple answers. Throughout the report an asterisk (*) denotes any value of less than half of one per cent but greater than zero.

All findings are based on weighted data, although unweighted base sizes have been provided.

Qualitative interviews

The reporting of qualitative findings deliberately avoids giving numerical values, since qualitative research cannot support numerical analysis. This is because purposive sampling seeks to achieve range and diversity among sample members rather than to build a statistically representative sample, and because the questioning methods used are designed to explore issues in depth within individual contexts rather than to generate data that can be analysed numerically.

Verbatim quotations and case illustrations are used to illuminate findings. They are labelled to indicate the job title of the interviewee, the size of SME, and whether the SME in question engages PAYE staff, self-employed staff or both. Further information is not given in order to protect the anonymity of research participants. Quotes are drawn from across the sample.

1   Profile of employment in SMEs

Chapter summary

This chapter explores the profile of employment in SMEs. It does this by quantifying the number and type of workers that SMEs employ, with a particular focus on the levels at which SMEs engage self-employed workers. Key findings are:

- 83 per cent of SMEs employ staff on a PAYE basis.
- 23 per cent of SMEs engage self-employed workers.
- 12 per cent of SMEs take on individuals through agencies.
- 66 per cent of SMEs only engage PAYE staff, six per cent only engage self-employed workers, and 17 per cent engage both PAYE and self-employed staff.
- SMEs engage self-employed workers for all different job roles, but most commonly for 'skilled professional' roles.
- 22 per cent of SMEs say that the number of people they engage varies throughout the year.

1.1   Current profile of worker classification

More than four in five SMEs employ staff on a PAYE basis (83 per cent). Around a quarter currently engage workers who are classified as self-employed (23 per cent) and 12 per cent of SMEs take on workers through agencies.[7]

| Figure 1:1 | Current profile of worker classification in SMEs |

Q. Are any of your staff employed on a PAYE basis?
Q. And are any of your staff currently classified as self-employed?
Q. Does... take on individuals through agencies?
% Yes
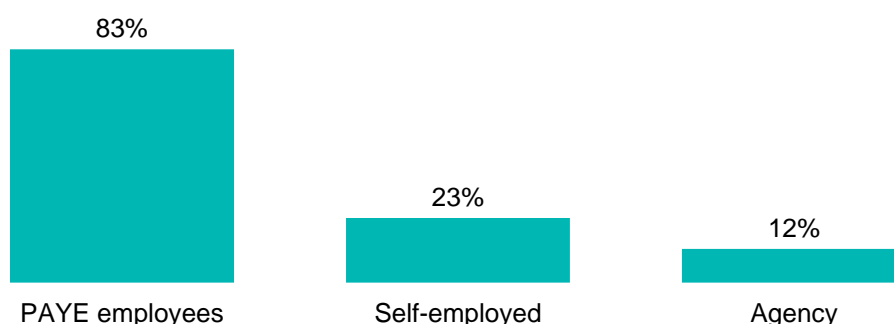
Base: All SMEs (n=1,722)

Larger SMEs are more likely to employ staff on a PAYE basis. Overall, 89 per cent of micro companies employ staff on PAYE terms, compared to 98 per cent of small businesses and 100 per cent of medium sized businesses.

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[7] Please note that these figures are based on all SMEs surveyed, including those who do not know the employment status of their staff. If these unknown cases are excluded the proportion that employs PAYE staff rises to 90 per cent, the proportion that employ self-employed workers rises to 25 per cent and the proportion which engage agency staff rises to 13 per cent.

Engagement of self-employed workers does not vary significantly according to the size of the business, but larger SMEs are more likely to take on individuals through agencies. While 11 per cent of micro businesses engage workers through agencies, this rises to 23 per cent of small businesses and 56 per cent of medium sized businesses.

Based on the type of staff employed by each SME, Figure 1.2 shows the breakdown of employer type. Overall, two in three SMEs only employ workers on a PAYE basis (66 per cent). Six per cent only have self-employed workers and 17 per cent employ workers on both PAYE and self-employed terms. The employment profile for one in ten SMEs is unknown.

If SMEs with unknown employment status are excluded[8], 74 per cent of SMEs only employ PAYE staff, seven per cent only engage self-employed staff, and 19 per cent engage both PAYE and self-employed workers.

Figure 1:2   Breakdown of employer type
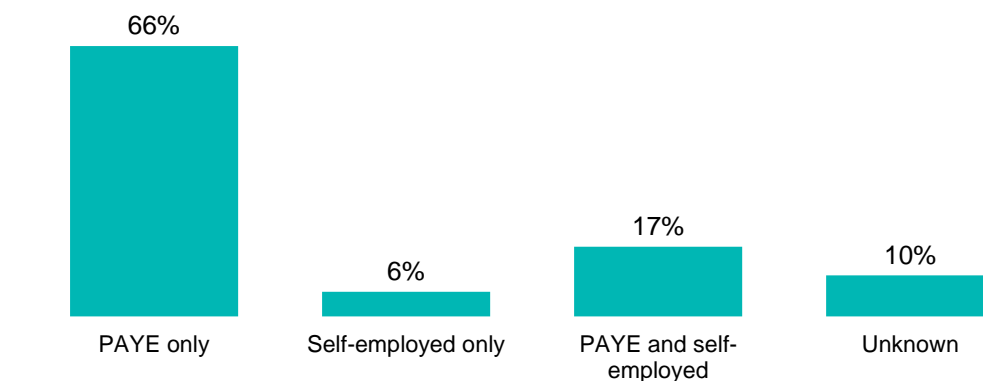
Base: All SMEs (n=1,722)

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[8] These are SMEs which do not know whether workers are engaged on PAYE or self-employed terms

1.2 Job roles of self-employed workers in SMEs

Figure 1.3 shows the type of roles that self-employed workers do in SMEs.[9] While SMEs engage self-employed workers for all different types of role, it is most common for self-employed workers to do roles in the middle of the occupational hierarchy. For instance, 30 per cent of SMEs which have self-employed workers engage skilled tradespeople on that basis. This is equivalent to seven per cent of all SMEs.

Similarly, a quarter of SMEs that engage self-employed workers do so for roles and tasks typically performed by professional staff (26 per cent, equivalent to six per cent of all SMEs). A similar proportion engage self-employed administrative or secretarial staff (23 per cent, equivalent to five per cent of all SMEs).

It is slightly less common for SMEs to engage self-employed workers at the extremes of the occupational hierarchy. Just 17 per cent of SMEs with self-employed workers engage managers, directors or senior officials on a self-employed basis (equivalent to four per cent of all SMEs), and the same proportion engage self-employed workers for elementary occupations.

Figure 1:3   Job roles of self-employed workers in SMEs

Q. Does your business take on self-employed people at any of the following levels or roles?

% Yes   ■ % SMEs with self-employed staff   ■ % All SMEs
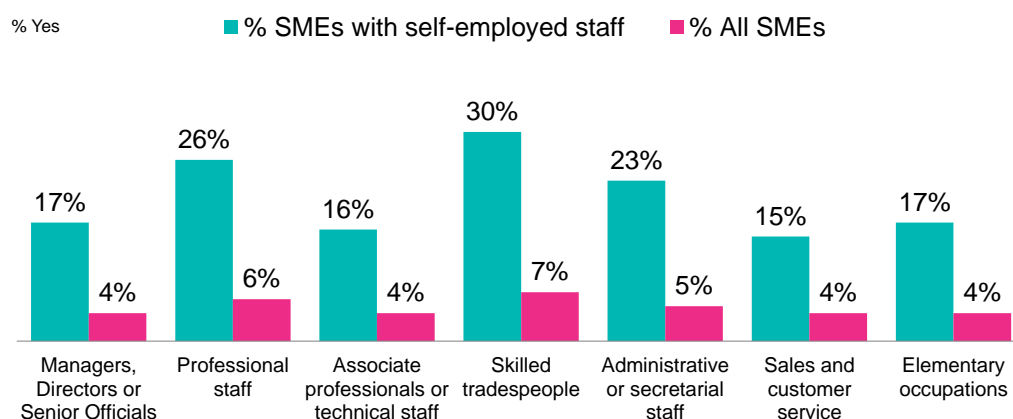
Base: All SMEs which have self-employed staff (n=334), All SMEs (n=1,722)

There is no significant difference in the job roles of self-employed workers based on the type of employer. That is, SMEs which only engage self-employed workers are no more or less likely to engage self-employed workers in specific roles than SMEs which engage both PAYE and self-employed workers.

The profile of self-employed workers also does not vary much across different sized businesses. However, the results indicate that medium sized businesses are significantly more likely than micro businesses to take on self-employed staff for associate professional/technical roles (14 per cent compared to 39 per cent).

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[9] The job roles are based on the ONS Standard Occupational Classification (SOC) Hierarchy. Clarification on the definition of these roles was given to all respondents who requested it.

Q. Does your business take on self-employed people at any of the following levels or roles?
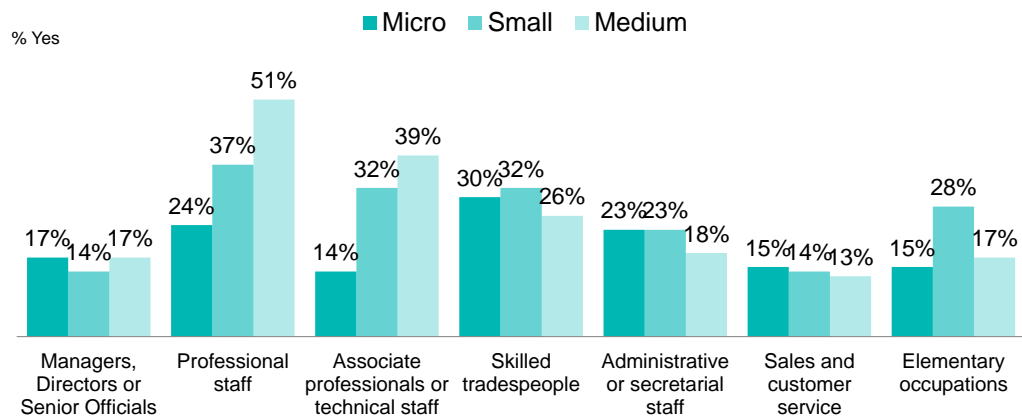
Base: All SMEs with self-employed staff (micro = 146; small = 102; medium = 71)

2 Determining employment status

Chapter summary

This chapter discusses the processes which SMEs go through when classifying staff, how confident they are in determining employment status, and any difficulties that they face. Key findings are:

- Responsibility for determining employment status varies across SMEs. In micro businesses, it is ordinarily the role of the business owner or managing director. In small businesses, it is commonly the role of a company secretary or operations manager. In medium sized companies, it tends to be the responsibility of a specialist such as a finance director or HR official.
- There are five main approaches to categorising employment status in SMEs: Only employing staff on PAYE terms; offering PAYE terms by default; giving staff a choice; making decisions on a case-by-case basis; and engaging staff on self-employed terms by default.
- As well as the nature of the role (length and type of work), SMEs consider a number of factors when determining employment status. These include if an individual has existing self-employed status; any risk to the business; the administrative burden; costs; and historic or industry practice.
- Virtually all SMEs are confident that they make the correct decisions when categorising the employment status of their workers (97 per cent). However, the qualitative interviews suggest that this confidence does not necessarily correspond with high levels of understanding of employment status, which are mixed.
- A lack of confidence can stem from one or both of the following: uncertainty about the distinction between employment status categories; or observed ambiguities between categories in specific workforce roles.
- Just one per cent of SMEs say they experience difficulties when categorising staff.
- When determining the employment status of an individual, 71 per cent of SMEs seek advice from an accountant, lawyer, or legal advisor.
- The difficulties SMEs describe range from experiencing uncertainty about employment status definitions to confronting more concrete situations, such as: when staff request an alternative classification; when self-employed staff carry out their work in the way employees typically do; and when HMRC had investigated employment status.
- Half of SMEs use guidance on the HMRC or GOV.uk websites (49 per cent) and 43 per cent contact HMRC staff directly.
- Four per cent of SMEs give staff a choice over their employment status, with two per cent doing so regularly.

2.1 Who categorises employment status within SMEs

The qualitative research shows that the staff member responsible for categorising employment status varies by business size. Typically, the smaller the businesses, the more involved business owners or leaders are in categorisation. For micro and small enterprises, business owners, Managing Directors (MD), and partners usually make decisions about employment status.

In small businesses, staff in leadership roles, such as the company secretary or operations manager, are sometimes responsible for categorising employment status. However, business owners or MDs tend to be consulted when challenging situations arise, such as when there was ambiguity around employment status criteria.

In medium sized businesses it tends to be senior members of staff, such as finance directors and HR officials, who are responsible for categorising employment status.

2.2 When categorising happens

Employment status tends to be categorised at three points, as illustrated in Figure 2.1 and explained in turn below:

Figure 2:1   When categorisation happens

When deciding staffing needs and defining roles

During recruitment and contract negotiations

After work has started - when staff ask to change employment status; when job roles change; when ambiguities arise in roles; and when contracts end and are re-negotiated.

Workforce planning   Recruitment   Contracted work
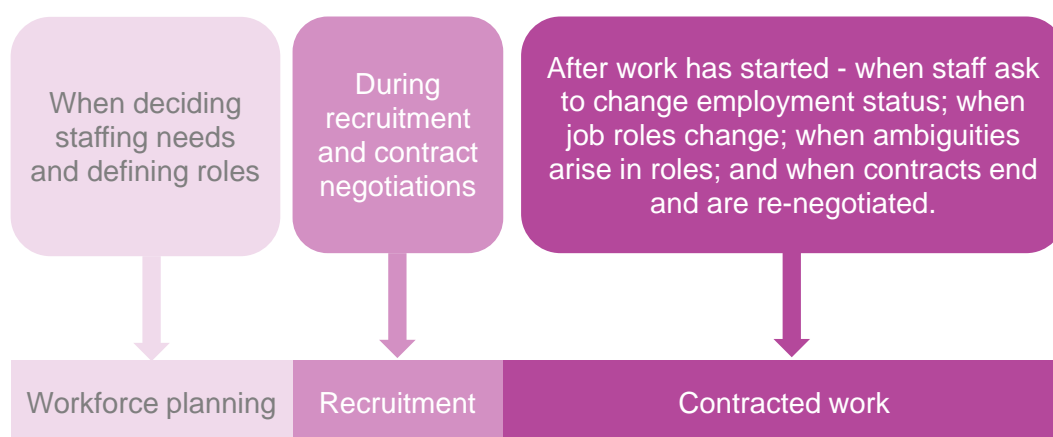
When decisions are made during **workforce planning,** SMEs consider employment status at the same time as determining new roles.

The following factors are considered by SMEs in relation to required roles: whether there is a long or short-term need for the role, the extent of specialism needed, how difficult the position might be to fill, and whether the individual would need to provide their own equipment.

For example, a medium sized housing association that engages both PAYE and SE staff makes decisions about employment status when they establish the roles needed in their workforce. If a specialist role is required, such as a project manager trained in energy efficiency, they would consider recruiting someone on a self-employed basis, whereas non-specialist or established salaried posts, such as administrators, customer service, or business support staff would be taken on as PAYE.

When decisions take place during **recruitment** as part of contract negotiations, SMEs might have received specific requests from prospective staff to be given a particular employment status. Alternatively, SMEs may offer potential recruits a choice of employment status. For example, a theatre company said that if someone applies for a fixed-term contract but wants to be a freelancer they would be open to discussion about how to categorise them.

'*Well when they come for the interview, they pass the interview and they've got the job they, in the interview they will tell me whether they're self-employed or want to go on to the books*'

Managing Director, Micro size business, Engages PAYE staff

Employment status is also sometimes categorised **after staff have started working for the business,** during service or when contracts end and are re-negotiated. Categorisations at this stage occur when staff request a change of employment status or challenge their status. For example, a SME, in this case a school, sought legal advice and revised an employment contract when a teacher challenged their self-employed status as they felt they should be on PAYE terms and should receive holiday pay.

Categorisations also occur at this stage when SMEs notice ambiguities in job roles, or when individuals' roles differ in practice to what was intended. For example, when a self-employed person appears to be performing the role of a PAYE employee, or in the way employees typically do (full-time, regular shifts), rather than the role they had been contracted to do. This can lead SMEs to question existing categorisations.

2.3 Approaches to categorising employment status

The qualitative research reveals five different approaches to categorising employment status. The extent to which SMEs go through a 'process' of active-decision making varies depends on the approach used. Where a decision is clear-cut, the process tends to be limited, whereas for others a more staged or iterative process, including discussions with the individual or management team and revisions to employment contracts, can take place. The different approaches are as follows:

Classifying staff as PAYE only

SMEs that engage all staff as PAYE do not identify with using a 'process' to categorise employment status. There are a number of reasons for the use of this approach.

A key driver behind this approach is that it is perceived to be the safer option in terms of being investigated by HMRC. In one example, a medium sized construction business put a policy in place to prohibit taking on any self-employed individuals. This action was taken in order to mitigate any risk of miscategorising staff due to lacking confidence in government rules on employment status.

Other SMEs that only take on PAYE employees do so because they have been advised to do so by their accountant, or because they understand this as necessary to adhere to sector-specific rules and regulations. For example, a healthcare company in Northern Ireland understood that they were unable to engage self-employed staff to comply with the requirement to monitor employees' work.

There are two further reasons why SMEs take this approach. The first is to ensure staff are treated fairly and feel part of a team. This is believed to result in better quality work. Secondly, and more exceptionally, engaging staff on a self-employed basis is avoided if SMEs lack the skills or understanding of how to process someone as self-employed. This occurred in a micro charity, in which the Treasurer believed some staff, for example church assistants and singers who provide services on an ad-hoc basis, could be classified as self-employed. However, he was not aware of how to set staff up as self-employed because the church used a payroll company to deal with such matters.

Some participants, however, cannot always explain why, particularly if they had joined the business after it was first established, or if the business had only ever operated using a PAYE system but without the participant knowing why,

> *'…because that's the way it has always been done'.*
> Accounts manager, small size business, PAYE staff

PAYE by default

SMEs taking this approach engage everyone automatically as PAYE unless self-employed status is specifically requested, including in cases where staff dispute their employment status. In such cases PAYE is the preferred option because it makes it easier to regulate pay and monitor hours worked, and is the safest option in case of an HMRC investigation.

> '*My default position, 'cause of my own wariness is always employee'*
>
> Director of business services, medium sized business, both PAYE and self-employed staff

Where requests arise, SMEs either leave it to the individual to decide on their preference or consider other factors, such as whether they are already set-up as self-employed and if they worked elsewhere. For example, one SME only agreed to engage individuals as self-employed if they passed a number of checks. The ESI tool was also used if the SME lacked certainty about the right course of action. The emphasis placed by SMEs on factors such as existing self-employed status suggests that they are weighting some factors incorrectly or disproportionately in their decisions.

A further motivation for these SMEs to engage staff on a self-employed basis is to make it easier to recruit specific roles, as this can often be difficult to do on a PAYE only basis. For example, an events company sometimes granted self-employed status to bar workers or general event workers because it was difficult to attract people if they refused self-employment.

Staff preference

Decisions about classifying employment status are informed primarily by staff preference if it is perceived as important for employment status to fit around staff needs and if the arrangement is not detrimental to the SME. As described in case illustration 2.1 below, factors such as local contexts can affect such decisions. In this case, a childcare provider in a very remote area offers staff a choice because people in the locality commonly work on a self-employed basis and are engaged in a number of jobs at a time. The SME believes it is helpful to offer staff a choice and say it makes no difference to the business itself.

The practice of offering staff a choice is also common in situations where SMEs are recruiting for very specialist roles and would have had difficulty securing staff without meeting their needs. For example, a SME that engages clinicians specialising in severe brain injuries says it would struggle to recruit these professionals without offering the option of self-employment because it is common for staff in these roles to carry out clinical work for statutory or other services too.

While individuals' preference is a key factor, SMEs still consider the benefits and drawbacks to the business and often require signs of existing self-employed status before engaging anyone on this basis (such as a Unique Tax Reference number). The process of agreeing employment status not only includes discussions with the individual, but some SMEs also use employment status checklists as a sense-checker.

The ESI tool is also used on occasions where the decision is not clear-cut. However if it is found to be unhelpful, staff preference is prioritised.

<div style="background-color:purple">

Case Illustration 2.1 – Offering staff a choice
Manager and proprietor at a small business, PAYE and self-employed staff

A childcare provider of 24 years, based in a remote area engaged PAYE staff at the time of interview but had taken on self-employed staff in the past. During the interview process for a new role, the SME proactively asked applicants for their preference of employment status. They said that in the local area people often worked as self-employed and were juggling jobs and having to fit these around study or childcare responsibilities. The participant understood that if somebody was taken on as self-employed they would already have a self-employed status and would hold qualifications in the childcare sector.

</div>

Case by case basis

SMEs that make employment status decisions on a case-by-case basis are open to either category and judge it on the nature of the role required. This often involves discussions between the management team regarding forthcoming roles. As discussed above, the following tend to be considered: the nature of the role and skills required, the hours needed, the regularity of the work, and the duration of it. For example, a farming business would consider taking someone on as self-employed if they require somebody to work for a short length of time, or require them to provide their own equipment. More exceptionally administrative burden is considered. For example, if short-term work is required the preferred option is to engage staff as self-employed.

Self-employed only or self-employed first

Engaging staff on a self-employed basis only was an approach undertaken by one SME in the qualitative sample. In the only example of this, this was due the SME, a horticultural company, believing it would be difficult to attract reliable staff without offering self-employment due to the low-take home pay in the industry. The participant in this case also avoided PAYE for ease, as the SME, a micro charity operating for nearly ten years had always used self-employed staff and did not have a PAYE system in place. The SME had previously been involved in an HMRC investigation around employment status, which resulted in self-employed outcomes for all staff. The person still however lacked certainty about the employment status of their staff and thought that because of the full-time hours they worked they could be considered an employee.

There is evidence of SMEs using self-employment to trial highly paid roles before making the decision to engage someone longer term on a PAYE basis. For example, a business took on a consultant on a temporary basis for three months with a view to employing them as PAYE if the role proved successful. This approach was financially motivated as the SME wanted to test out whether paying a high salary on a longer-term basis was warranted.

2.4 Factors informing decisions

The factors informing SMEs' decisions regarding employment status include the nature and requirements of the job; advice and guidance; whether potential staff are already set up as self-employed; risk and regulation; administrative burden and costs; historic or industry practice; and employee choice. These factors are discussed in turn below:

The requirements of the job

Across the sample of SMEs participating in qualitative interviews, decisions about employment status are informed by established factors associated with employment and self-employment. The factors cited are listed in table 2.1, alongside the characteristics generally associated with different employment status categories, though there are exceptions:

Table 2:1	Characteristics associated with employment status categories	
Factors considered	**PAYE**	**Self-employed**
Length of contract	Long-term	Short-term
Regularity of work	Regular	Irregular
Number of hours	Greater	Fewer
Autonomy over hours	Less autonomy	More autonomy
Control over the way work is done	Less control	More control
Provision of equipment and tools	By employer	By staff
Extent of specialism	Less	More
Place of work	Up to employer	Up to staff
Monetary risk	Employer	Staff
How pay is decided	Less control	More control
Substitution	No	Yes

There is great variation in which characteristics take precedence in decisions, as this depends on the nature of the business and specific requirements of the role. However, there were a number of characteristics, described below, which were consistently mentioned by SMEs during the qualitative interviews as key perceived determinants of employment status.

SMEs considered the length of the role and the **regularity and number of hours** worked as key characteristics when categorising staff. If staff were working for a SME for a considerable period of time, or were working regular or nearly full-time hours SMEs associated them with PAYE status.

Autonomy in choosing when to work, and **control** over the way work was done were also strongly associated with self-employed staff.

Self-employed, they, they usually, you know, they make their own decisions. They do the job that, er - you know, I ask them to come and do a job and they do that job but they're, they're left to do it. Whereas PAYE, […] I ask them what to do and oversee -see what they're doing.

Partner in business, micro business, both PAYE and self-employed staff

In addition, the **provision of equipment and tools** by a staff member was consistently described as a characteristic of self-employed staff. For instance, the ownership of equipment and tools was an important factor in a micro horticultural and tree surgery company interviewed, which required staff to provide their own specialist tree climbing kits and therefore only take on self-employed tree surgeons. However, not providing their own equipment did not necessarily mean a staff member was categorised as PAYE as in exceptional cases the nature of the work meant self-employed staff could not be asked to provide their own equipment. For example, a self-employed art teacher was not expected to provide her own equipment due to the risk pupils may damage it.

Advice and guidance

SMEs describe seeking the following information and guidance on employment status:

- ESI tool
- HMRC help line
- GOV.uk
- Internal or external HR/Payroll
- Accountants
- Lawyers
- Colleagues
- Peer businesses

Advice from HMRC, accountants and lawyers is often sought to determine employment status in cases where PAYE staff members wish to be classified as self-employed in order to check they are making the right decision. In such cases the legal advice received helps to confirm their decisions to continue engaging staff on a PAYE basis.

SMEs tend to consult the GOV.uk and HMRC website if they want to check they are doing things correctly, or when difficult situations around employment status arise. The GOV.uk and HMRC website might be used in the first instance, before resorting to other information sources such as the ESI tool, legal information, accountants) if further clarity is required. Other websites that SMEs consult include Acas and the Federation of Small Businesses, particularly for legal queries.

Colleagues and peer businesses tend to be consulted when SMEs are uncertain about employment status decisions in specific circumstances. One example was when changes to a staff member's personal circumstances required them to work flexible hours and the SME wanted advice about this. Advice from colleagues and peers is also sought around outcomes of the ESI tool, particularly when SMEs do not have confidence in the outcome.

Advice is sought from internal or external HR/Payroll when decisions are being made about taking someone new on and in what capacity they should do so.

Existing self-employed status

Among SMEs engaging self-employed staff, decisions to engage staff on this basis are often underpinned by whether there is evidence that the worker is already operating as self-employed. It is common for SMEs to seek confirmation that the person has their own business and is carrying out work elsewhere. The types of information SMEs consider as 'evidence' of self-employment include a business name, references, National Insurance number, and Unique Tax Reference (UTR). The UTR in particular is perceived, albeit incorrectly, to be a good indicator of self-employment because it suggests that they report their income for tax purposes.

> *'…the easiest way to prove that you're self-employed is your unique tax number isn't it?'*
>
> Managing Director, Micro sized business, Both PAYE and SE

For other businesses, the main indicator is if the person is working elsewhere and does not have one single main employer. This information is commonly sought via references.

Invoicing is considered a further indicator of whether someone is genuinely self-employed. There are examples of SMEs requesting invoice templates before work starts, or examining invoices in detail on receipt, checking for whether they are VAT registered. It was through checking the invoice template of a self-employed staff member that led a farming business to believe that the individual was not genuinely set up as self-employed. After seeking advice from an accountant the SME put the individual on the PAYE system and the individual subsequently left. The SME later received a letter from HMRC explaining that the individual had not submitted tax returns for two years.

Risk and regulation

Risk is a further factor in decisions to engage staff on a PAYE or self-employed basis.

SMEs describe protecting themselves by avoiding taking on self-employed staff in case individuals do not report their income to HMRC. Some SMEs are wary of this because they cannot guarantee that the person is reporting their income and think this could lead to financial penalties for the business. For example, a small events company preferred to classify staff as PAYE in case self-employed staff were not paying their tax and NI contributions, therefore risking fines to the SME from HMRC. In addition, decisions to classify staff as PAYE, either as a blanket policy, by default or in response to confusion about the right course of action, are motivated by the desire to avoid the risk of fines in the event of an investigation.

In contrast, self-employment is seen as less of a risk for the business if the volume of work is unpredictable or if it is not known whether a new role will work for the business as discussed in Section 2.2.

Adherence to sector specific rules and the ability to monitor and regulate employees' work, discussed above, are further drivers to PAYE categorisations.

Administrative burden and costs

Administrative burden

Administrative burden and costs such as taxes, pension and holiday pay are not widely taken into account by participating SMEs when deciding the employment status of staff. There are only limited examples of businesses that take administrative burden and costs into account and they tend to be micro or smaller businesses that do not have processes and personnel, such as HR or payroll staff, in place for processing staff.

Where the administration around categorising employment status does influence decisions, one reason, experienced by micro sized businesses, is a reported lack of skills or knowledge around processing the alternative status (this is discussed further in 2.2). The length of engagement is also a factor: businesses that are influenced by administrative burden prefer to take on short term or ad hoc staff as self-employed because it is administratively easier. For instance, a language school only engaged self-employed teachers due to the risk that they will not stay long term. The perceived effort involved in setting up a pension, holiday or maternity pay for short-term staff is considered disproportionate by the SME.

> *'I don't have time to spend the whole of my life talking to an accountant setting up a pension for someone who may or may not stay for more than a fortnight'*
>
> > Owner and Business Director, Micro sized business, both PAYE and SE staff

Costs

SMEs tend to be aware of the costs associated with employment status decisions, including costs of market rate pay, holiday pay, sick pay, pensions, tax, training, and security checks. For example, self-employment could be seen to be the cheaper option because it removes these costs and because a fixed rate of pay can be agreed in advance. However, whether self-employment or PAYE is considered the more expensive option varies according to SME and their specific circumstances and concerns.

It should be noted that awareness of these costs does not necessarily shape employment status decisions. In the limited situations in which it does, a key consideration is the presumed financial repercussions of being found to mis-categorise employment status by HMRC. Engaging staff as PAYE is considered the cheaper option here.

There are also limited examples of savings on salaries and entitlements shaping decisions. For example, employing a person as PAYE is seen as the cheaper option in cases where fixed-rate fees have been set independently to ensure fair pay for freelance workers in particular sectors. Self-employment is also an attractive option to avoid the costs of tax, sickness and holiday pay or to avoid committing to engaging a highly paid role on a permanent basis

Historic or industry practice

Some participants' decisions are based on existing organisational practices. These participants do what their business or sector has always done, but without personally understanding employment status categories or knowing why they categorise in that way. For example, a small mortgage intermediary business that engages both PAYE employees and self-employed staff explained that mortgage brokers are traditionally self-employed across the industry. Those that categorise in this way are not necessarily confident in their decision.

Employee choice

As discussed above, in some cases decisions about classifying employment status are informed by staff preference. In these instances, the choice has little impact on businesses, or helps support staff recruitment, particularly specialist roles. Choice is offered with the use of checks to verify existing self-employed status. In some cases if an individual is unable to prove their SE status, they would be engaged as an employee. SMEs also consulted available guidance such as employment status checklists and the ESI tool to validate decisions.

2.5 Confidence in categorising staff

Overall, the quantitative survey shows that SMEs tend to be confident that they are making the correct decisions when categorising the employment status of their workers. Four in five say that they are *very* confident (82 per cent) and a further 15 per cent say that they are *fairly* confident. Just one per cent of SMEs say that they are not confident when categorising staff.

Figure 2:2	Confidence in categorising staff

Q. Regardless of whether you use the HMRC Employment Status Indicator tool, how confident, if at all, are you that your business is making the correct decisions in assigning staff as PAYE employees or as self-employed?

Not very confident: 1%

Don't know

2%

Fairly confident

15%

Confident
97%

82%

Very confident

Base: All SMEs (n=1,722)
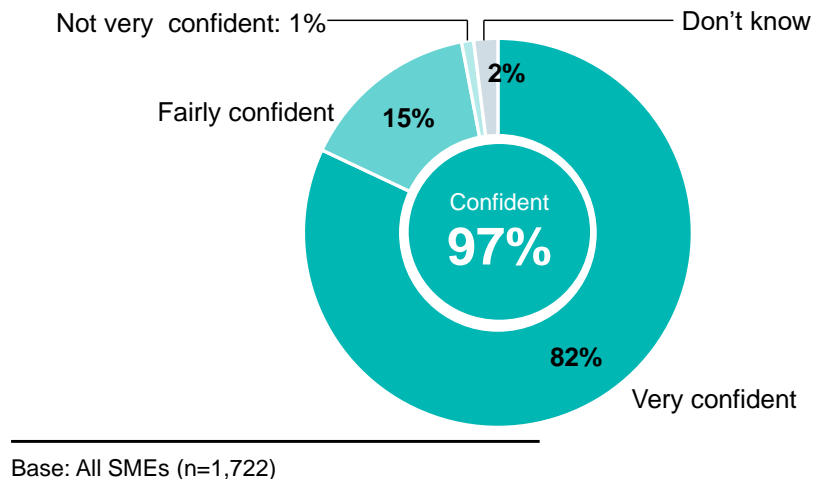
Levels of confidence in categorising staff do not vary significantly according to the size of the business, SIC category, or nation. Levels of confidence also do not vary significantly based on whether the business engages only PAYE, only self-employed, or both PAYE and self-employed workers.

However, it may be that these high levels of confidence are gained in retrospect, that they are the result of receiving support from professional advisers, for instance.

The views of SMEs reporting that they are not very confident in their employment status categorisations were explored in the in-depth interviews. This reveals that a lack of confidence can stem from one or both of the following:

• Uncertainty about the distinction between employment status categories; or

• Observed ambiguities between categories in specific workforce roles.

While some of these SMEs could offer reasons for their decisions, they were not completely confident that their categorisations would stand up to scrutiny.

Uncertainty in the distinction between employed and self-employed categories

Some feel that their understanding of employment status definitions and the differences between them is not sufficient to determine confidently whether their organisational practices are correct. See case illustration 2.2 below.

> **Case illustration 2.2 – lack of confidence in employment status categorisations due to uncertainty about definitions**
> Micro business, PAYE staff
>
> An operations manager in a change control management business said she could not be confident in the SME's decisions because she lacked an in-depth understanding of employment status categories, and what distinguished one from another. This participant had a basic understanding of entitlements and conditions associated with self-employment, such as the absence of holiday or sick pay and autonomy over hours. The SME engaged specialist staff on a short-term SE basis as a kind of trial period to test individuals' performance and the suitability of new roles. They intended to make staff permanent employees if they performed well but due to these roles being highly paid did not want to risk engaging them longer term if the role did not work out.

Uncertainty about the distinction between employment and self-employed often occurs when decision makers in SMEs lack experience determining employment status. Two types of participant fit this description. The first include those who are new to the business and therefore lack experience or knowledge about the staff profile within the business. The second include business owners who experience difficulties while employing staff for the first time or who have never employed someone in a role that may be considered as self-employed.

Lack of confidence in correct decision making is also influenced by other businesses in the same industry making alternative decisions about employment status. For example, a SME explained that while they were confident they should take on staff as employed for specific roles, prospective staff had told them other businesses took them on as self-employed.

Observed ambiguity in specific roles

Overlaps or 'grey areas' between characteristics associated with being employed and self-employed are a common cause for SMEs' lack of confidence in employment status decisions. SMEs experiencing this range from those with a basic to good understanding of employment status definitions. Even those with a good understanding find 'grey areas' and are unsure about which characteristics, if any, should take precedence in classifications. This instils doubts about their practices and about whether others, such as HMRC, would see things in a different way.

A common issue that causes confusion and inhibits confidence is the length of a person's employment contract (see case illustration 2.3 below). As mentioned in section 2.4, length of contract is a factor consistently taken into account by SMEs in their decisions about employment status. SMEs nonetheless report uncertainty about whether longevity of work should take precedence over other characteristics of employment such as using their own tools or flexibilities of when worked could be carried out. Confusion can arise both in circumstances where SMEs engage short-term and long-term staff as the case illustration above demonstrates.

SMEs also report finding the number of employment status criteria and scenarios in guidance and tools (including the ESI tool) confusing. Their confidence can be affected by the feeling that the right course of action in relation to ambiguous roles is too open to interpretation, or that a slight change in employment circumstances could result in a different status.

In such cases, SMEs appear to go with what suits the organisation or employees best.

SMEs that are confident in their categorisations

SMEs that report feeling confident about categorisation feel they have a full enough understanding of employment status definitions and the distinctions between them, think decisions are clear cut within their workforce, or have sought advice from a professional. This group is discussed further in the next section.

2.5.1 Understanding of employment status definitions

High levels of confidence in employment status definitions do not necessarily correspond with similarly high levels of understanding. The qualitative research identifies three broad levels of understanding of employment status definitions:

Good understanding

SMEs that fall into this category have a strong understanding of the differences between PAYE employees and self-employment. These SMEs often consult HMRC guidance or the ESI tool in relation to challenges or uncertainty experienced in the past.

However, even SMEs with a good understanding of employment status definitions experience confusion and lack confidence around categorising staff when there is overlap or ambiguity between different criteria in relation to specific workforce roles. This is discussed further in section 3.4.

Moderate understanding

SMEs with a moderate understanding of employment status definitions are informed in part by government employment status definitions, but also by assumptions based on past experiences or observations of different employment status categories. This means that these SMEs are not confident their understanding and workplace practices are correct. Again, a key challenge for this group is determining the right course of action in cases of overlap in employment status criteria.

Little to no understanding

SMEs in this category have never fully considered employment status definitions, or express confusion or uncertainty about the differences between categories.

> *'It's such a big subject that I don't think anyone really knows like for certain what makes someone self-employed or PAYE"*
>
> Operations Manager, micro size business, PAYE staff

SMEs in this group include those who are unable to explain the reasons for their categorisations due to following historic practice rather than actively making the decision themselves. Others take advice from accountants or solicitors, or have categorised according to individuals' preference without consulting other sources.

These SMEs are often initially confident in their decisions because they are following previous practice or advice. However, participation in the interview led some SMEs to question their own knowledge and motivated them to reassess organisational practices with the use of available guidance and tools.

2.6 Difficulties in categorising staff

Just one per cent of SMEs say that they have had difficulties when classifying staff as either PAYE or self-employed. As with confidence, however, it is possible that these perceptions are gained in retrospect and may reflect use of guidance, or not fully understanding employment definitions.

Figure 2:3 Difficulties in categorising staff

Q. Does your business ever have any difficulties in deciding whether an employee should be classified as PAYE or self-employed?

Don't know: 1% — Yes: 1%

98%

No

Base: All SMEs (n=1,722)
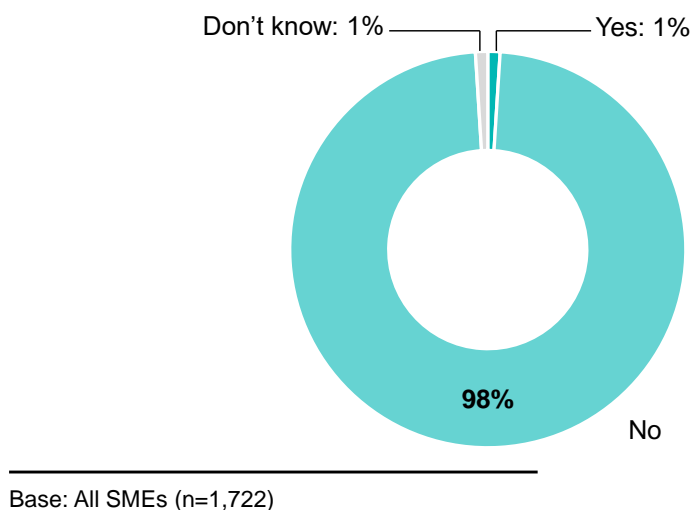
While a large majority of all sub-groups report no difficulties, medium sized bodies are more likely to report difficulties than micro businesses (four per cent compared to one per cent).

SMEs operating in agriculture, forestry and fishing (eight per cent), arts, entertainment and recreation (seven per cent), and human health and social work (six per cent) are also significantly more likely to experience difficulties in classifying staff.

The experiences of SMEs reporting that they <u>had</u> experienced difficulty categorising employment status were explored in in-depth interviews. The difficulties SMEs describe range from experiencing uncertainty about employment status definitions to confronting situations that are more concrete. The situations experienced centre on:

- When staff request an alternative classification
- When self-employed staff carry out their work in the way employees typically do, and
- When HMRC had investigated employment status.

Staff requests for alternative classifications

Requests from existing or prospective workers for an alternative employment status are challenging when SMEs are uncertain about the right course of action. This occurs when SMEs lack understanding of employment status definitions and / or when there are perceived overlaps between categories. An assessment of roles, in conjunction with advice from colleagues and professionals, and use of guidance and tools such as the Employment Status Indicator, help to shape decisions.

SMEs that had declined requests to change to self-employment wished to avoid the risk of mis-categorisation, and wanted to retain control over the place, hours and types of work undertaken. Two case illustrations for this, 2.4 and 2.5, are given below.

Case illustration 2.4: difficulties arising from staff requests to change employment status
Small business, both PAYE and self-employed staff

A landscaping and civil engineering company received a request from a temporary PAYE employee to become self-employed. They found the decision difficult, primarily because the participant who was in charge of accounts and payroll was new to the role and was unsure of employment status definitions. Although the individual worked on a temporary basis, they decided with advice from the business owner to keep the employee on PAYE because they wished to retain control over the types and locations of work he did.

Case illustration 2.5: difficulties arising from staff requests to change employment status
Small business, both PAYE and self-employed staff

An events company, trading for over 5 years in the hospitality sector reported receiving regular requests from prospective staff about working on a self-employed basis. The SME experienced difficulty categorising particular roles, such as bartenders, because of the ambiguity in their role. For example, they are told what to do and for how long in the same way as employees, but are required to provide their own tools e.g. bottle openers, cocktail shakers. The SME's preference was to process all staff as employees in order to avoid the risk of mis-categorisation. However, they recognised that sometimes requests to be self-employed may be justified.

In situations where staff requests had been accepted, the difficulty of recruiting specialised roles was a key consideration. In one case, an artist in residence at a special school wished to be engaged on a self-employed basis. The SME's preference was PAYE due to the requirement to work a prescribed number of hours and at specified times and the provision of equipment by the school. In other respects, the school could, however, see the artist as self-employed. For example, they would paint

their own works while on site that they would then sell and had some extent of control over the way they worked.

In this case, the SME was not completely confident in either classification but used the ESI tool to shape the contract to ensure it reflected a self-employed role. However, the SME still lacked confidence in the decision because of the overlap in categories. In other cases, safeguards were put in place to protect the business when a self-employed status was granted, such as enforcing as a period of leave and a rotation of clients.

Some SMEs find it challenging when staff request to switch between statuses but perform exactly the same role. A healthcare business experienced this situation when self-employed individuals lost other avenues of work and wished to move to PAYE or vice versa.

When self-employed staff work in the way employees are perceived to

SMEs report difficulty determining employment status correctly when they perceive staff to conduct work in ways they associate with the alternative status (see case illustration 2.6). The SMEs describing this situation consider a range of factors to determine employment status such as the regularity and duration of the role, control over working hours, extent of direction or instruction given, and the provision of tools. In these cases, the decisive factors appear to be the regularity and duration of the roles, the number of hours worked or the control over the hours worked.

Case illustration 2.6: difficulties arising from ambiguities in employment status
Small business, PAYE staff only

A small coach driving business trading for eight years occasionally took on temporary coach drivers to cover staff shortages. The Managing Director said he found it difficult to determine whether a staff member should be classified as employed or self-employed in these instances. Their preference was to engage staff as employees because of the reduced cost of pay and expenses, but they took drivers on as self-employed if they were engaged elsewhere on a self-employed basis. On one occasion, a temporary self-employed driver steadily began working more and more hours. This raised doubts about the drivers' self-employed status. The SME consulted peers within the industry, and an accountant, and the staff member was moved to PAYE. Furthermore, the SME decided to categorise all staff as employees because they lacked confidence about the distinction and did not want to risk making a mistake.

When HMRC had investigated employment status

The qualitative sample includes two participants with experience of HMRC investigations into employment status. Being investigated led these SMEs to revise their approach to classifying staff and focused their minds on the overlap between categories. In one case, a participant had been found in a previous business to have categorised staff incorrectly after accepting specific requests for self-employment. This participant now operates a PAYE only policy.

In the other case, the SME continues to engage staff on a self-employed basis only, based on the HMRC outcome agreeing the classification, but operates strict requirements. This includes the requirement for prospective staff to register as self-employed and provide their unique tax reference number. This participant still has doubts about employment status in these cases because workers are engaged long-term and full time.

> *'I've got subcontractors working for me but in theory I am employing them nearly on a full-time basis. […]In theory they all should be employees'*

> Micro business, self-employed staff only

2.7 Processes SMEs follow when categorising staff

There are a number of actions that businesses can take to minimise the risk of making a mistake in categorising workers. These include taking advice from various sources, using agencies (where the agency acts as the employer) and taking out insurance.

2.7.1 Taking advice from government or professionals

As Figure 2.4 shows, the most common action for SMEs when categorising staff is taking advice from an accountant, lawyer, or legal advisor. Seven in ten SMEs seek this kind of professional advice (71 per cent).

More than half of SMEs use government advice or guidance. For instance, 49 per cent use guidance on the HMRC or GOV.uk websites, and 43 per cent contact HMRC staff directly. Combined, 59 per cent of SMEs do at least one of these things and 25% do both.

Overall, 76 per cent of SMEs take advice, either from a professional or from government. This rises to 83% among those that only employ PAYE workers and 93% that engage both PAYE and self-employed workers. However, businesses that only engage self-employed workers are significantly less likely to take advice from a professional or from the government (59%). Indeed, 41% of SMEs which only engage self-employed workers do not take advice on the status of their workers.

Figure 2:4 Taking advice from government or professionals

Q. Does your business do any of the following things when categorising people as either PAYE employees or self-employed…

% Yes

71%	49%	43%	59%	76%
Take advice from an accountant, lawyer or legal advisor	Use guidance on the HMRC or GOV.UK websites	Contact HMRC staff, either by phone, email, letter or in person	Take advice from government	Take advice from professional/ government
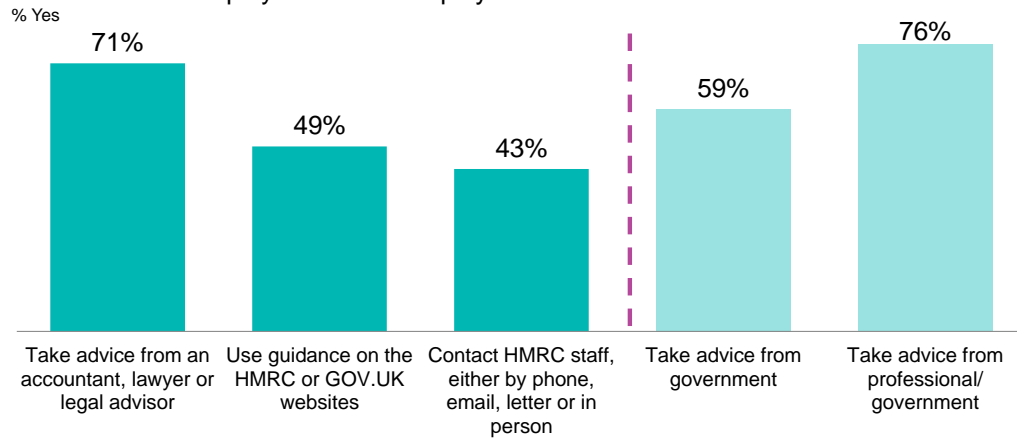
Base: All SMEs with at least one employee (n=1,638)

As Figure 2.5 shows, there is relatively little variation in the actions that SMEs take based on their size. The main difference is observed when it comes to using governmental guidance. Larger SMEs are more likely to use the guidance provided on the HMRC or GOV.uk websites (73 per cent of medium sized businesses use these channels, compared to 47 per cent of micro businesses).

Figure 2:5 Taking advice from government or professionals by business size

Q. Does your business do any of the following things when categorising people as either PAYE employees or self-employed…

% Yes

■ Micro ■ Small ■ Medium

70% 75% 73%	47% 59% 73%	42% 44% 51%	63% 68% 82%	82% 84% 86%
Take advice from an accountant, lawyer or legal advisor	Use guidance on the HMRC or GOV.UK websites	Contact HMRC staff, either by phone, email, letter or in person	Take advice from government	Take advice from government/ professional
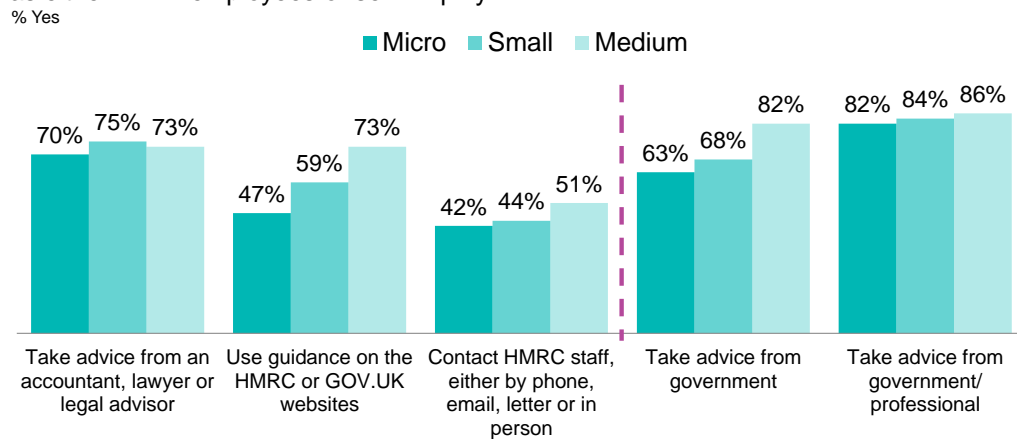
Base: All SMEs with at least one employee (n=1,638)

Businesses based in Scotland are also significantly more likely to use government guidance on the HMRC or GOV.uk websites (70 per cent, compared to 47 per cent in England and 44 per cent in both Wales and Northern Ireland), although the reasons for this are unclear.

2.7.2 Taking out insurance and offering staff a choice

Just under one in five SMEs take out insurance to help with costs in the event of an HMRC investigation (18 per cent).[10] [11]

Only a small minority of SMEs use agencies to provide staff to avoid having to categorise them (two per cent) or offer staff a choice of their job status (four per cent).

Figure 2:6   Taking out insurance and offering staff a choice

Q. Does your business do any of the following things when categorising people as either PAYE employees or self-employed…
% Yes

| 18% | 2% | 4% |
| Take out insurance to help with costs in the event of an HMRC investigation | Use agencies to provide staff in order to avoid having to categorise staff | Offer staff a choice between joining as a PAYE employee or being self-employed |
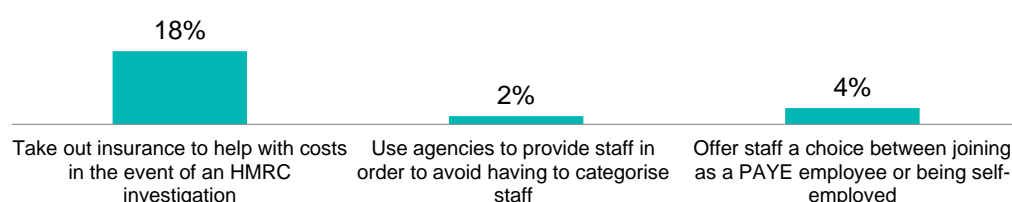
Base: All SMEs with at least one employee (n=1,638)

While only four per cent of SMEs offer staff a choice over their employment status, this does vary depending on the type of work they do. SMEs operating in the Arts, entertainment and recreation sector are the most likely to offer workers the choice of work status (23%), and construction bodies are also significantly more likely to do so (nine per cent).

Among SMEs that do offer staff a choice on their classification (four per cent), around half say that they always do (46%) and a further 21% say that they do sometimes. This equates to two per cent of all SMEs offering staff a choice of employment status at least some of the time. The other two per cent only offer staff the choice rarely, or do not know how often they do so.

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[10] Read-out instruction for interviewers at this question: 'This refers to insurance you have taken out specifically for investigations around employment status and not general insurance in the event of other HMRC investigations.'

[11] The qualitative interview included respondents to the quantitative survey that said they had taken out insurance to cover the costs of an investigation into employment status. However, when probed the types of insurance they described were general forms of insurance to cover any issues associated with tax or being an employer, rather than employment status specifically. Examples include employer or public liability insurance and insurance for tax investigations, in one case as part of membership with the Federation of Small Businesses. As such, the actual proportion of SMEs taking out specific insurance for investigations into employment status classification may be lower.

Table 2:2	Whether businesses offer staff a choice of employment status, and how regularly	
Base: respondents from businesses with at least one employee: n=1,638		*% (weighted)*
Does [BUSINESS NAME] ever offer staff a choice between joining as a PAYE employee or being self-employed?		
Yes		4%
No		91%
Don't know		5%
Base		*100%*
Base: respondents whose businesses offered staff a choice between joining as a PAYE employee or being self-employed: n=70		*% (weighted)*
How often would you say that [BUSINESS NAME] offers staff a choice between joining as a PAYE employee or being self-employed?		
Always		46%
Sometimes		21%
Hardly ever		29%
Never		1%
Don't know		3%

2.8 Presence of risk factors

One of the aims of this research is to identify the proportion of SMEs which are at risk of mis-categorising the employment status of their workers. While there is no way of definitively measuring the impact of certain actions or processes on the likelihood of mis-categorisation without a control sample of businesses known to mis-categorise, it is possible to quantify the number of risks that businesses are exposed to.

Prior to the research, six 'risk factors' were identified through discussions between NatCen and the relevant HMRC research and policy teams. These are behaviours or actions which, it is hypothesised, could increase the risk of mis-categorisation because they are likely to introduce a subjective component in the decision, be associated with lower level of understanding of the rules, or be associated with more complex cases. These are:

- Not using governmental online guidance;
- Not contacting HMRC staff;
- Not taking professional advice;
- Not currently using the ESI tool;
- Taking out insurance to help with costs in the event of an HMRC investigation; and
- Giving staff a choice over their employment status.

Each of these actions are given a score of one, and they are then aggregated for each SME, to give a score between zero and six. The higher the number, the more risks that

a business takes. (Businesses with an unknown number of employees were given a score of zero.)

It should be noted that this approach is only one possible way of calculating the risk of mis-categorisation of employment status. Indeed, this approach has a number of areas for refinement. In particular, the current scoring gives equal weight to each of the actions (that is, not seeking professional advice is given the same score as giving staff a choice, for instance). In reality, some actions are likely to be more or less closely correlated to mis-categorisation.

Further, it is possible that in some instances one step is all that is required to categorise with confidence (for instance, using HMRC guidance may be deemed sufficient) and therefore SMEs which do this but do not perform any further actions may be scored unfairly highly using this system.

Indeed, the qualitative interviews suggest that SMEs that were extremely confident in the action(s) they have taken to ensure they are categorising employment status correctly do not access other resources. For instance, if an SME has a legal consultant or an accountant who advises them on employment status, they may not consider using other sources of information. However, as this pattern of behaviour was not discussed explicitly during the interviews this is an assumption about the behaviour of the SMEs interviewed based on the available information,

Figure 2.7 shows the distribution of scores using this calculation. Under this approach, the mean score is 2.2 out of six, with most SMEs scoring below this (60%). It could be assumed, therefore, that those with a score of three or above have a higher than average risk of mis-categorising the employment status of their staff. (It is worth noting, however, that no SMEs scored six.)

Figure 2:7   Presence of risk factors

Base: All SMEs (n=1,722)
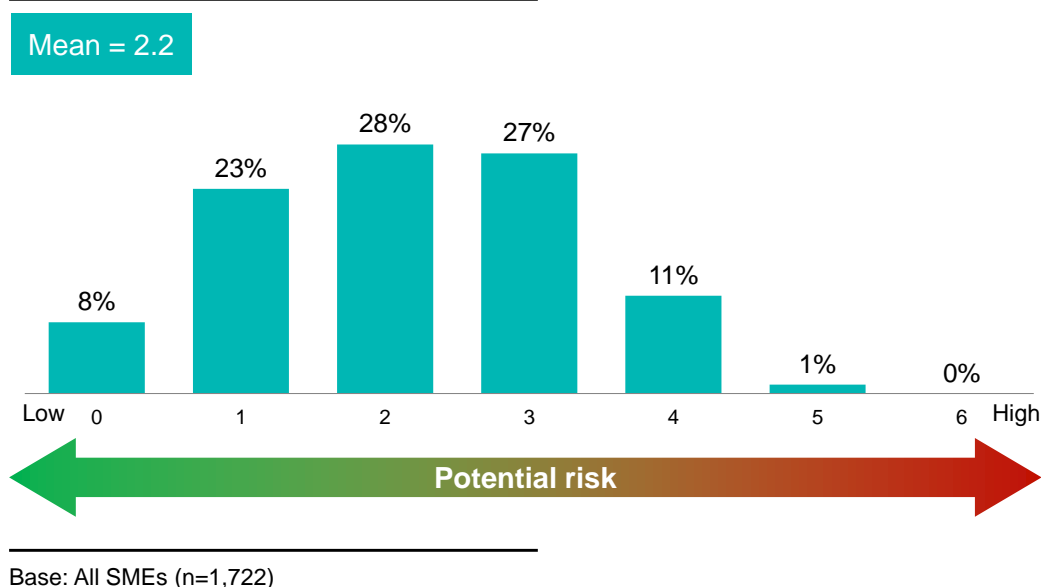
The most commonly occurring risk factor is not currently using the ESI tool. Overall, based on the whole sample, 90% of SMEs do not currently use the ESI tool. This is followed by not contacting HMRC staff (47%), not using HMRC guidance (38%), not

taking professional advice (22%), taking out insurance (15%) and offering staff a choice (three per cent of all SMEs).[12]

Figure 2.8 breaks down the presence of risk factors by the type of employer. It shows that, on average, SMEs that only engage PAYE workers have a slightly higher number of risk factors than those which engage self-employed workers. However, this finding is not statistically significant, so this difference could be down to chance.

Figure 2:8   Presence of risk factors by employer type
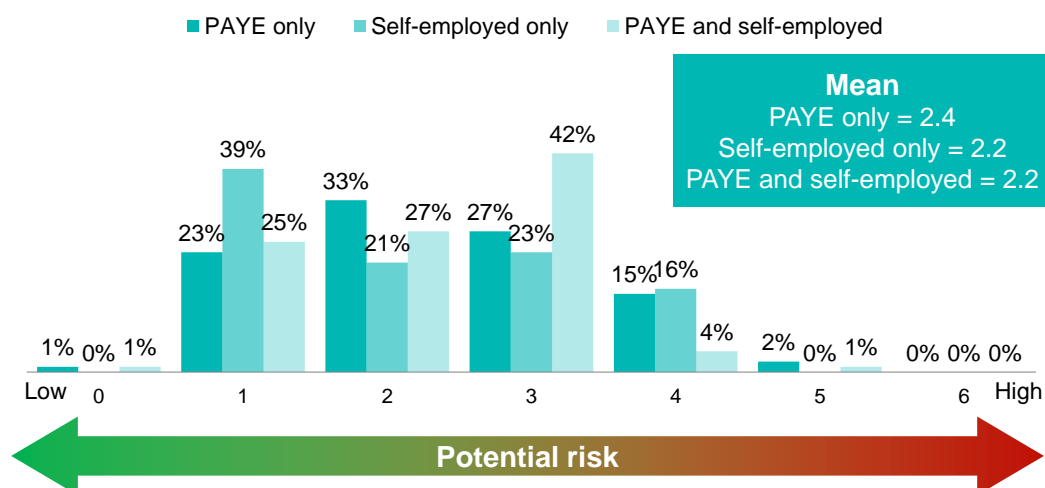
Base: All SMEs (n=1,722)

Based on this model, 40% of SMEs have a higher than average risk in classifying their staff. Table 2.3 compares the profile of SMEs with a higher than average number of risk factors with the profile of all SMEs. This shows that there are no significant differences in the profile of the two groups. That is, prevalence of higher risk does not appear to be influenced by the size of a business, the sector it works in, the type of employer, or the age of the business. Instead, prevalence of risk appears to be spread evenly across the population of SMEs.

Table 2:3	Profile of higher risk groups compared to overall profile of SMEs	
	All SMEs *(Base: n=1,722)*	**SMEs with higher than average risk factors** *(Base: n=673)*
Employment band		
Micro	86%	88%
Small	11%	10%
Medium	2%	2%

---

[12] Please note that these figures are based on all SMEs, not just those known to employ staff. As such, the figures given in this paragraph are slightly different to those discussed in section 2.7.

	All SMEs *(Base: n=1,722)*	**SMEs with higher than average risk factors** *(Base: n=673)*
Employer type		
PAYE only	66%	71%
Self-employed only	6%	6%
PAYE and self-employed	17%	20%
Nation		
England	84%	85%
Scotland	8%	8%
Wales	5%	5%
Northern Ireland	3%	2%
Age of business		
Under 5 years	20%	14%
Over 5 years	79%	85%
Industrial classification		
A - Agriculture, Forestry and Fishing	3%	3%
B,D,E - Mining and Quarrying; Electricity, Gas and Air Conditioning Supply; Water Supply	1%	1%
C – Manufacturing	6%	7%
F – Construction	12%	10%
G - Wholesale and Retail Trade; Repair of Motor Vehicles and Motorcycles	15%	17%
H - Transportation and Storage	4%	4%
I - Accommodation and Food Service Activities	6%	8%
J - Information and Communication	9%	6%
K - Financial and Insurance Activities	2%	2%
L - Real Estate Activities	4%	3%
M - Professional, Scientific and Technical Activities	13%	14%
N - Administrative and Support Service Activities	11%	13%
P – Education	2%	2%
Q - Human Health and Social Work Activities	5%	4%

Table 2:3 Profile of higher risk groups compared to overall profile of SMEs

Table 2:4 Profile of higher risk groups compared to overall profile of SMEs (continued)

Table 2:3	Profile of higher risk groups compared to overall profile of SMEs		
R - Arts, Entertainment and Recreation		2%	2%
S - Other Service Activities		5%	5%

However, it should also be noted that a business with a higher number of risk factors may not actually be at any more risk than businesses with a lower number of risk factors. That is, in straightforward cases where all employees are automatically given PAYE status, it is likely that a business would take relatively few steps to confirm the classification. They would therefore score highly in this model, despite being low risk. However, it is equally fair to assume that that business is not taking steps to reduce what little risk they face.

3 The Employment Status Indicator tool

Chapter summary

This chapter focuses on the Employment Status Indicator (ESI) tool. In particular, it looks at awareness and use of the tool, user experience, and confidence in the outcomes it produces. It also explores ways in which SMEs feel the tool could be improved. Key findings are:

- 24 per cent of SMEs are aware of the ESI tool.
- 5 per cent of SMEs have used the ESI tool and 2 per cent currently use it.
- The tool is most commonly used to address any uncertainty SMEs have over an individual's work status, particularly in complex cases.
- Those who do use the tool tend to be positive about it: 79 per cent say that it makes it easier to make the right decision when classifying workers and 94 per cent say that it is easy to use.
- While SMEs tend to find the tool useful, it is not normally relied upon to definitively determine employment status and is often used in conjunction with other sources.
- One reason for this is a lack of confidence in the outcome that the tool produces.
- While 35 per cent of users are very confident that the tool gives the correct decisions, 25 per cent are only fairly confident and 10 per cent are not confident.
- Uncertain results also reduce confidence in the tool, and 17 per cent of users have experienced an uncertain result. Most who have this experience default to classifying individuals as PAYE workers.
- Despite this, the tool is generally seen as useful and 83 per cent of users would recommend the tool to other businesses.
- Key suggestions for improving the tool include using plain English (if not possible, explaining complex terms); for similar questions emphasising key words of differentiation; ensuring response options cover all eventual scenarios; routing users based on their business type to questions relevant to them and providing more detailed information about a given outcome.

HMRC provides guidance for businesses and individuals in the form of the Employment Status Indicator (ESI) tool. This is a set of guidance plus an interactive online tool that is designed to help businesses and individuals to understand whether they should classify staff as employees or self-employed.

3.1 Awareness of the ESI tool

Overall, one in four SMEs are aware of the ESI tool (24 per cent). This consists of 18 per cent which recognise the tool based on just its name (unprompted awareness) and a further six per cent which are familiar with it when prompted with a description of the tool.

Figure 3:1   Awareness of the ESI tool

Q. Have you ever heard of HMRC's Employment Status Indicator tool – the ESI?
It doesn't matter whether you have actually used it.

Awareness by sub-group

All	24%
Micro	23%
Small	28%
Medium	38%
England	22%
Scotland	32%
Wales	24%
N. Ireland	43%
PAYE only	25%
Self-employed only	23%
PAYE & Self-employed	19%

Base: All SMEs (n=1,722)
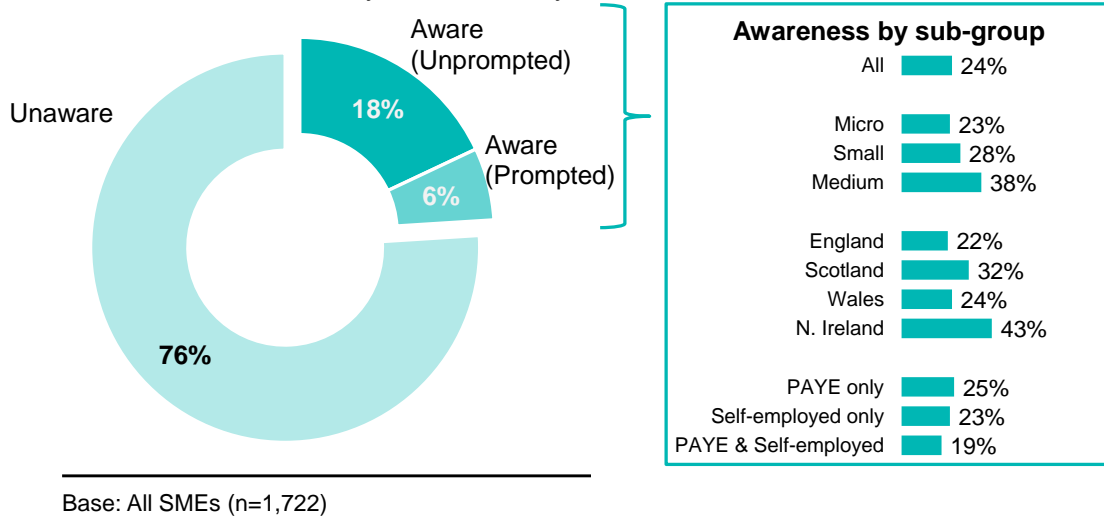
Awareness of the ESI tool is significantly higher among medium sized companies than micro companies (38 per cent compared to 23 per cent). There is also regional variation in awareness, with SMEs in Northern Ireland significantly more aware of the ESI tool than those in England (43 per cent compared to 22 per cent).

3.2 Use of the Employment Status Indicator tool

Among those which have heard of the ESI tool, one in five have actually used it (20 per cent). This is equivalent to five per cent of all SMEs in the UK. Use of the ESI tool largely reflects awareness levels, being higher among medium sized businesses than among micro businesses (18 per cent compared to four per cent).

Figure 3:2   Use of the ESI tool

Q. Have you ever used the HMRC Employment Status Indicator tool at [BUSINESS NAME] or at a previous business?

Use of ESI tool by sub-group

All	5%
Micro	4%
Small	7%
Medium	18%
England	4%
Scotland	9%
Wales	4%
N. Ireland	8%
PAYE only	5%
Self-employed only	3%
PAYE & Self-employed	6%

Base: All SMEs which have heard of the ESI tool (n=463); All SMEs (n=1,722)
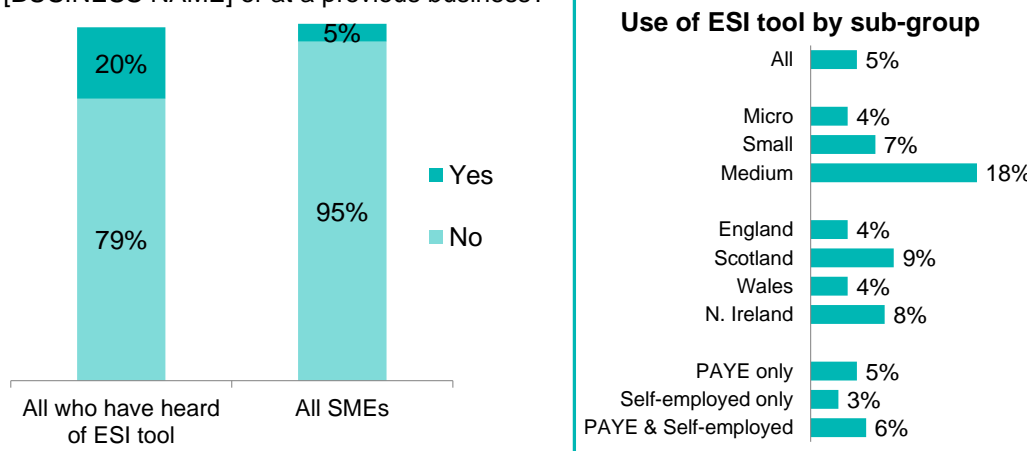
There is also some variation by the sector in which SMEs operate. Specifically, use of the ESI tool is highest among businesses in the arts, entertainment and recreation sector (19 per cent) and those which operate in the services sector (15 per cent).

Use of the ESI tool is also higher in younger businesses. Among businesses aged up to five years, nine per cent have used the tool, compared to four per cent of businesses aged over five years.

Among SMEs which have used the tool, 44 per cent currently use it. This equates to two per cent of all SMEs being current users of the tool.

3.2.1 Reasons for using the ESI tool

The qualitative research suggests that the most widespread reason for using the tool is to address uncertainty about categorising employment status. In such cases, the tool is used in one of three ways:

- **As guidance in particularly difficult cases**. For example when a staff member challenges their employment status or requests to be re-classified (see case illustration 3.1 below for more details);

- **To ensure that the working practices of staff who request to be categorised as self-employed meet HMRC's criteria for self-employment**. In one case a participant used the tool repeatedly to shape the working conditions of a future member of staff to ensure they could be considered self-employed; and

- **To confirm current practices** in relation to categorising employment status.

Those who use the tool because they are unsure about employment status appear to use it in conjunction with other sources of information and advice, such as the HMRC help line, employment status checklists, and Acas. Non-governmental sources of information – such as private employment consultants; HR advisors; and networks made up of similar businesses – are also used by some SMEs.

> **Case Illustration 3.1 – Use of the ESI tool in difficult cases**
> *Micro business, with both PAYE and self-employed staff.*
>
> A staff member who had reached the end of their fixed term contract with the business asked if it was possible for them to become self-employed. They were considered self-employed by their other employers, and felt it might be easier to be self-employed for all of their work. The managing director felt unsure if this was appropriate given the staff member's working arrangements. Of particular concern was the amount of work the staff member received from the SME, as they were working for them for the majority of the year. The SME used the tool, which gave an inconclusive answer. This result, along with a phone discussion with HMRC, and the SME's HR advisors, confirmed that the situation was borderline, so the SME could take the course of action that worked best for both parties.

In more exceptional cases, some individuals have used the tool to achieve a desired employment status for an employee, or to prove their own employment status to employers.

Case illustration 3.2 Using the ESI tool to achieve a desired employment status
Medium business, both PAYE and self-employed staff

In one case, a school engaged a self-employed therapist. All of the other therapists working at the school were employees and the SME's preference was to engage staff on a PAYE basis to avoid repercussions for miscategorising. The therapist in question was recruited at a time that the school was in urgent need of a therapist, and when it was difficult to secure staff with the required skill level. The therapist agreed to the role but only on a self-employed basis because she wanted control over her working hours. The SME agreed to this but was reluctant due to the remuneration costs of employing the therapist on a self-employed basis. The SME was also doubtful because they saw many similarities between the role of the self-employed therapist and her employed counterparts. In addition, the ESI tool came up with an employed result. The school subsequently consulted colleagues about the nature of the role and reassessed some of their answers after which they achieved a self-employed outcome.

'*That one was a lot harder and I don't think I made the right decision but it - we got it to fit with the tool so I went with it in the end. It was - it was a situation of making - making the situation fit the tool rather than the tool determining that that was an appropriate way to go. Not something that we would do again.*'

3.2.2 Reasons for never using the ESI tool

SMEs which are aware of the ESI tool but have not used it tend to cite a lack of need (44 per cent), or only employing staff on a PAYE basis (32 per cent). Less common reasons for not using the tool are using other professional advice (16 per cent) or already understanding how to classify staff (10 per cent).

Figure 3:3   Reasons for not using the ESI tool

Q. Why have you never used the HMRC Employment Status Indicator tool at [BUSINESS NAME]?

Never had need to use the ESI tool — 44%
We only employ people on a PAYE basis — 32%
We use an accountant to decide whether people should be PAYE or self-employed — 16%
No staff/not applicable — 15%
Always known how to classify — 10%
No reason — 8%
Other — 17%
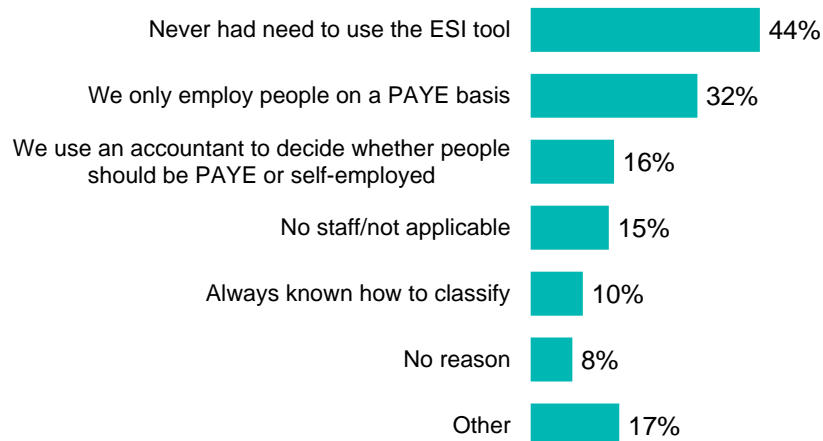
Base: All SMEs who have heard of the ESI tool but do not use it (n=318)

3.2.3 Reasons for not using the ESI tool more often

SMEs that have used the ESI tool, but do not always use it, give similar reasons for not using it more often. The most commonly cited reason is that it is not considered necessary. For example, 24 per cent of this group say that all staff are PAYE, while 22 per cent simply say they have no need to use the tool.

A small minority cite negative experiences of using the tool (nine per cent) or unreliable answers (four per cent).

Table 3:1 Reasons for the business not currently using the Employment Status Indicator tool (/more often)	
Base: All who have used the tool and whose business do not currently always use the ESI tool: n = 125	*% (weighted)*
Can you say why your business does not use the Employment Status Indicator tool [more often]?	
All staff are PAYE / don't take on self-employed	24%
No need / not applicable	22%
Use an alternative process for determining employment status	14%
No change in staff / low turnover	10%
Miscellaneous negative views and experiences of ESI tool	9%
Confident about determining employment status	7%
ESI tool answers are not reliable	4%
No employees	4%
Other reason	6%
No reason	1%
Don't know	2%
Base	*100%*

3.3 User experiences of the ESI tool

SMEs which have used the ESI tool tend to be positive about the experience. For instance, four in five say that the ESI tool makes it easier to make the right decisions when classifying workers (79 per cent). Indeed, as Figure 3.4 shows, 54 per cent say that the ESI tool makes classification *much* easier. However, a small but notable minority feel that the ESI tool actually makes classification of workers more difficult (nine per cent).

Q. To what extent would you say that the Employment Status Indicator tool makes it easier or more difficult for your business to make the right decisions when classifying workers – would you say the ESI tool…

Don't know **11%**

Makes it somewhat more difficult **9%**

Easier: **79%**

Makes it much easier to make the right decisions about employment status **54%**

Makes it somewhat easier **25%**
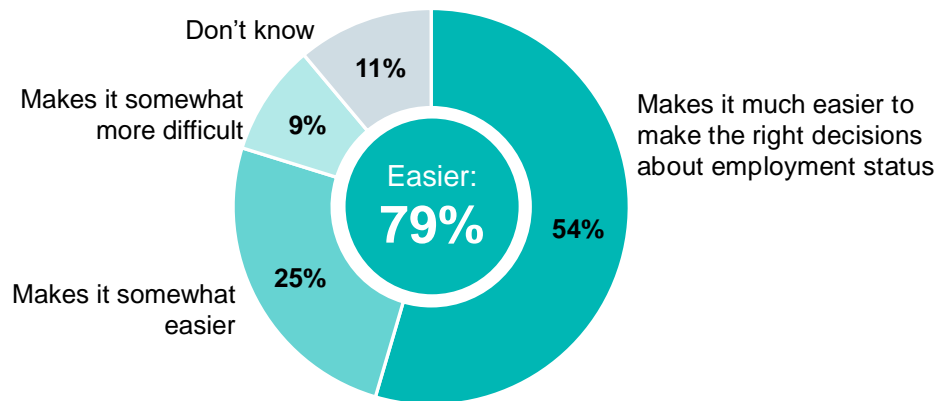
Base: All who have used the ESI tool (n=140)

SMEs are similarly positive about the usability of the ESI tool. Among users of the tool, virtually all feel that it is easy to use (94 per cent), with just under half saying that it is *very* easy (46 per cent).

Further, 77 per cent find it easy to understand the questions in the ESI tool. However, six per cent of users say that the questions are difficult to understand.

Figure 3:5 Usability of the ESI tool

■ % Don't know/It depends ■ % Very difficult ■ % Fairly difficult ■ % Fairly easy ■ % Very easy

How easy or difficult do you find using the ESI tool?
3 3 | 48 | Easy: 94% | 46

How easy or difficult do you find it to understand the questions in the ESI tool?
18 | 6 | 38 | Easy: 77% | 38
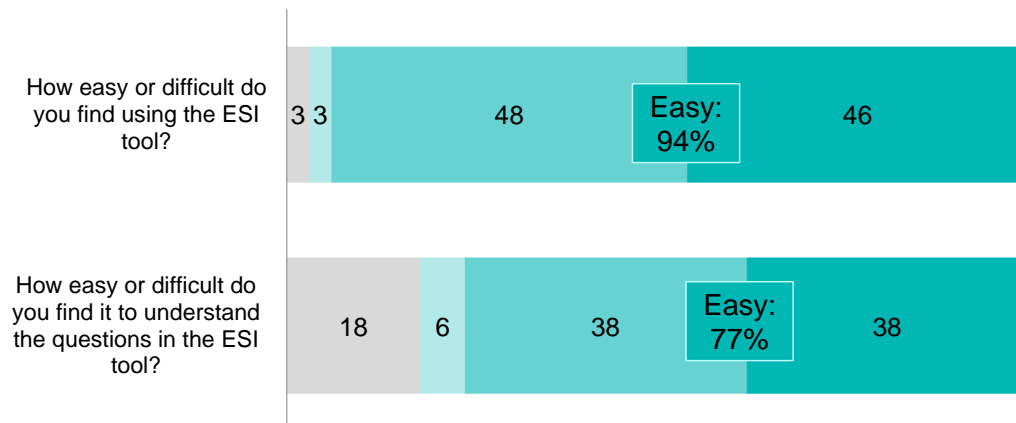
Base: All who have used the ESI tool (n=140)

3.4 Confidence in the ESI tool

The qualitative research suggests that while SMEs use the ESI tool to address uncertainty – and those who use it find it to be a valuable resource – it is not relied upon to definitively determine employment status. This is largely due to a lack of confidence in its results which stems from perceptions of the tool as a useful source of guidance rather than a conclusive outcome.

Indeed, confidence in the outcomes that the tool produces is fairly low. This is supported by the quantitative research which shows that while a majority of users are confident that it gives the correct decision (61 per cent), only 35% are *very* confident. Further, a relatively large minority are actively not confident (10 per cent) and 30 per cent are unsure.

Figure 3:6 Confidence in ESI tool outcomes

Q. When you get the results from the Employment Status Indicator tool, how confident, if at all, are you that the tool is giving the correct decision in categorising an individual as an employee or as self-employed – would you say you are…

Very confident
Don't know/It depends 30%
35%
Confident 61%
Not at all confident 4%
Not very confident 6%
25%
Fairly confident
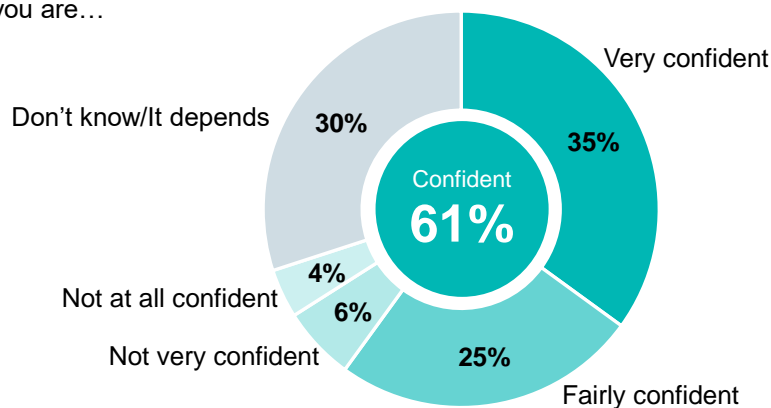
Base: All who have used the ESI tool (n=140)

The qualitative research suggests that a number of factors can lead to low-confidence in the tool's outcomes. For instance, there are those who lack confidence in the outcome of the tool because they are worried that they have given **incorrect or inaccurate answers**.

> *'If I've answered the questions wrong it doesn't really mean anything does it? It's a self-assessment, which is only as good as the person doing it.'*
>
> HR manager, medium business, PAYE staff and self-employed staff

This is related to the answer options available in the tool. There are instances when none of the available answers are perceived to accurately represent the scenario the SME is testing, and this can raise concerns about the outcome.

This view appears to relate both to questions which force users to answer 'other', and to questions which do not take into account the SMEs' business situation. For instance, questions about when work has to be done which do not take into account seasonal fluctuation.

> '*It's not gonna give a true answer because we're being forced to kind of tick things that aren't quite … exact.*'
>
> Managing director, micro business, PAYE and self-employed staff

A key improvement suggested by participants is ensuring that there are enough question options to allow users to accurately reflect the realities of their employment situation. One suggestion is that the tool should route users based on their business type so that the questions would be relevant to their circumstances.

Another factor leading to low confidence in the tool is a lack of clarity in some questions, which means that there are those who feel that **some questions can be misinterpreted or answered in more than one way**. These questions can increase concern that the outcome is not reliable. One SME suggested that this means the tool could be manipulated to achieve the answer they want.

A further explanation for a lack of confidence in the tool is experiencing **uncertain or unexplained outcomes**, where the tool does not give a clear indication of employment status. The qualitative research shows that uncertain outcomes can make participants feel they have not gained anything by using the tool.

The quantitative research shows that these uncertain outcomes are relatively common. As Figure 3.7 demonstrates, 17 per cent of ESI tool users have experienced this kind of uncertain outcome. When SMEs experience an uncertain result, the most common reaction is to categorise the worker as PAYE (63 per cent), while a quarter take further professional advice (25 per cent).

The qualitative research suggests those who are unsure about the outcome of the tool are influenced by factors such as whether they are able to give accurate answers; if the tool gives a response which conflicts with their existing knowledge; and if the tool gives an indeterminate outcome. These are discussed in more detail below.

Figure 3:7   Proportion of ESI tool users experiencing an uncertain outcome

Q. Have you ever used the HMRC Employment Status Indicator tool and had an uncertain result, that is, where the ESI tool output says that it is not possible to determine whether a person should be categorised as an employee or as self-employed?
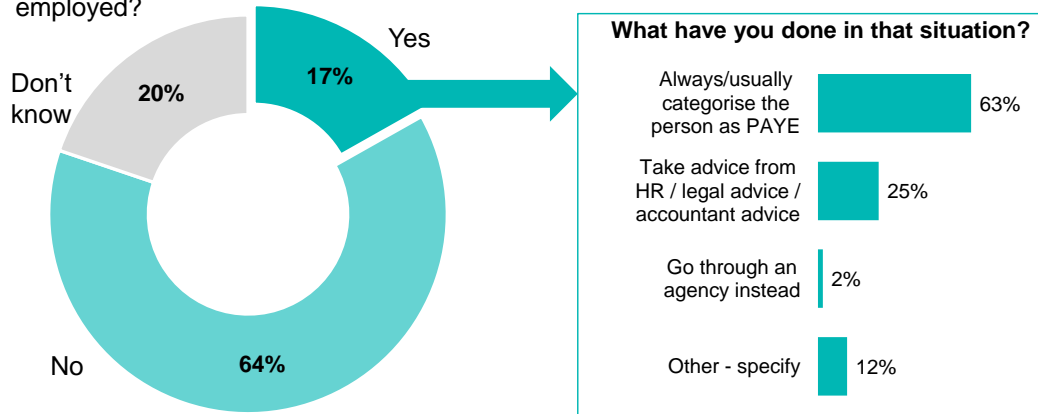
Base: All who have used the ESI tool (n=140)

A further factor driving low confidence in the tool is it producing **unexpected outcomes**. These challenge participants' understanding of employment status, without necessarily explaining why their understanding is incorrect.

Again, the quantitative research shows that unexpected results are fairly common. While three in five say that they *always* understand the results the tool produces (62 per cent), one in five users say that they only *sometimes* understand the results (19 per cent) and one per cent *rarely* understand the results. When those who are unsure are excluded, 22% of users only sometimes or rarely understand the outcomes from the tool.

Figure 3:8   Understanding of ESI tool outcomes

Q. And when you get the results from the Employment Status Indicator tool, do you understand why the tool has given a particular result? Would you say you…
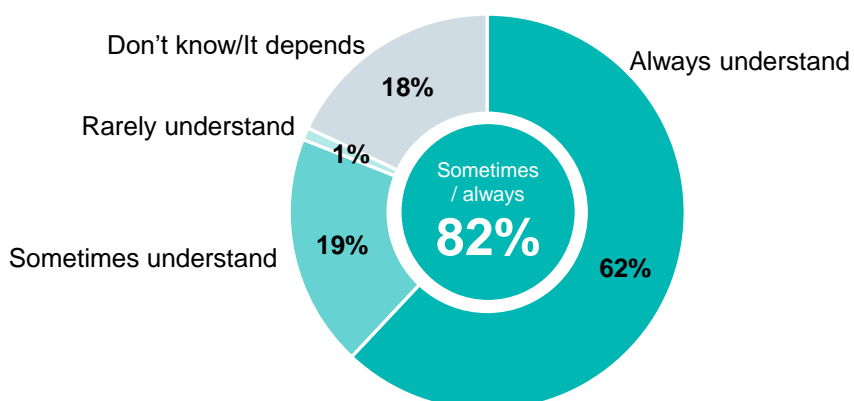
Base: All who have used the ESI tool (n=140)

The in-depth interviews suggest that SMEs that do not fully understand the reasons behind an outcome do not tend to have confidence in it.

> *'It tells you a kind of yes/no answer but really what you want to understand is the reasoning why.'*

> Managing director, micro business, PAYE and self-employed staff

It was suggested that the tool could be improved by providing more detailed information on the outcome page about why a status was given, and explaining more thoroughly the complex terminology used on the outcome page.

In contrast, confidence in the tool is largely driven by confirmation of existing decisions and the official status of the tool (see case illustration 3.3). For these participants, the tool is reassuring and a useful way of checking decisions they have made. One participant explained that they would not have felt confident in the outcome if they had not got the answer they had expected.

Case Illustration 3.3 – Trust in the ESI tool due to its official status
Micro business, both PAYE and self-employed staff

In this case the SME had a dispute with a staff member concerning their employment status. The staff member accused the SME of incorrectly categorising them as self-employed, and suggested they were owed backdated holiday pay. The participant, who was the founder and business director, was very concerned as they had a number of staff members categorised in the same way, and did not think they would be able to afford backdated holiday pay. The tool, along with a discussion with Acas and an employment consultant, reassured the SME that they had made the right decision. The participant felt partially confident in the outcome they received from the ESI due to the official status of the tool. As demonstrated by the quote below this confidence was also reliant on referring to other sources in addition to using the ESI tool.

'*I have faith in this. You know I've answered it honestly, so if this has been designed by the government barristers and all the rest of it then I'm assuming it must be okay. I've spoken to someone from Acas. They support it. I've spoken to a lady from a law firm or she's a paralegal […] and she was reasonably confident that what I was doing was, you know fair and proper and legal.'*

While users do not necessarily use the tool for a definitive result, on balance most users would recommend the tool to similar businesses (83 per cent). Indeed, 58 per cent say that it is *very* likely that they would recommend the tool. However, a substantial minority say that they would not be likely to recommend the ESI tool (17 per cent).

Q. How likely, if at all, is it that you would recommend the HMRC Employment Status Indicator tool to other businesses like yours?
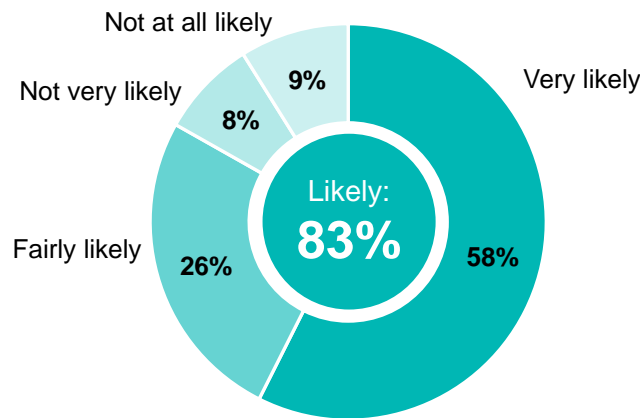
Base: All who have used the ESI tool (n=140)

3.5 User testing

In order to explore views on the use of the tool in more detail, this research included a user-testing element. This consisted of face-to-face interviews with 10 individuals working in 11 SMEs. Seven of the participants had used the ESI Tool prior to the user testing; three had not used the tool before. Participants were selected initially on the basis of having previously used or heard of the ESI Tool. In the later stages of recruitment after the sample of those who had used or heard of the ESI Tool had been exhausted a small number of SMEs were included who had not used or heard of the tool. All of those interviewed fit the selection criteria used for the qualitative sample. The SMEs covered a range of sectors, including education, health care, the arts, charity, construction, and media. All SMEs engaged only PAYE staff, or both PAYE and self-employed staff. There were three micro businesses, four small businesses and four medium businesses.

3.5.1 Locating and accessing the ESI Tool

The ESI tool was easy to find. Participants either searched for the tool on GOV.uk, or used a search engine. They were confident they had found the tool successfully when they recognised the official HMRC page on the gov.uk website. Generally, participants did not read the introduction page before using the tool. A number of participants did not even look at the introduction page.

> *"In a normal situation, it's like reading the terms and conditions on your mobile phone contract. I mean no-one does it do they?"*
>
> > Founder and business director at a micro business, both PAYE and self-employed staff

Those who did had the following comments:

- There was too much information on the introduction page

- The text was small and the page looked old fashioned

- The number of caveats listed on the introduction page was high. This prompted the feeling that the tool was not going to be very useful, especially for participants who had experienced difficulty answering some of the questions.

- The link to the tool at the bottom of the introduction page was perceived to be difficult to find due its size.

> *'Well, it's so small, isn't it? It's ridiculous'*
>
> Finance manager, small business, PAYE staff only

Participants suggested the link should be made more obvious, perhaps through adding a different colour, or making the text bold.

3.5.2 Accessing help and guidance

Those who accessed the help pages in the tool had mixed experiences.

Participants who found the pages helpful stated that they clarified complex terminology for them, or gave useful examples. In contrast participants who did not find the pages helpful felt that they did not clarify issues of confusion. For instance, the help pages still used complex terminology that the participant did not understand, and the pages did not provide any new information.

> '*You still won't understand it by pressing on the question mark 'cause it just says it again in language that you don't necessarily mean anything and it doesn't really give you more information*'
>
> HR manager, medium business, both PAYE staff and self-employed staff

A number of participants did not use the help pages. Reasons for this included believing that a help button was unlikely to help them understand what answer choice was applicable to their situation, and finding similar help buttons had not been useful in other scenarios.

It was suggested that access to help could be improved. For example, participants felt that the help buttons should not open onto a different page because it makes the tool slower and more cumbersome. A possible solution suggested by participants was for the help information to appear if the user hovered their cursor over the question mark.

Participants also wanted it to be easier for users to talk to advisors if they need more information or help using the tool.

Most participants did not use the further guidance pages. One participant who did found the information provided confusing, as terminology used on the guidance page e.g. agency worker, was not fully explained.

3.5.3 Look and layout of the tool

The look and layout of the tool was considered generally acceptable, but there was room for improvement. Reference was made to other HMRC tools which had a better layout, such as the Statutory Maternity Pay tool and the Statutory Sick Pay tool.

The absence of a back button caused frustration among participants who could not move backwards through the tool without losing a session. Users wanted to be able to do this to understand the logic of the tool; for instance, why similar questions were

being asked regarding worker substitution, and to check what answers they had given to previous questions.

> '*You can't go back. Okay, that's annoying I can't go back to check. Is it because I didn't answer properly or is this slightly different wording?*'
>
>> Director of business services, medium size business, all PAYE staff

Adding a status bar was suggested to resolve the issue of not having a back button, as it would allow users to see their previous answers and understand how their answers would influence the outcome of the tool

It was thought that the font should be larger and easier to read and that the graphics and colours were old-fashioned. One participant stated that it would improve the user-experience of the tool if the graphics were modernised.

3.5.4 Language

Views on the language used in the ESI tool varied between participants. One view was that the language was generally straightforward and that the tool did not expect users to have expertise in payroll or HR.

However, less positive views of the language used in the tool were widespread among participants. The questions were seen as complicated and not written in clear English. It was common for participants to re-read questions during the user testing as they had difficulty understanding their meaning.

Participants also felt the tool used very complex terminology and did not provide sufficient explanation of what terms meant, even if users referred to the help pages.

> '*…for someone like me, I regard myself as reasonably intelligent and educated, but if you're not familiar with the legalese it just doesn't mean anything to you… if it gives you some examples then I think that would help*'
>
>> Founder and business director at a micro business, both PAYE and self-employed staff

A key recommendation for improving the tool was to avoid complicated terminology. If using complex terminology is unavoidable, HMRC should ensure that the help pages provide sufficient explanation of terms.

3.5.5 Problem questions in the ESI Tool

Participants who found the questions straightforward and easy to answer had a more positive experience of using the ESI tool. It was unclear why some SMEs found the tool easier to use than others.

There was widespread confusion around certain questions, described in turn below. Participants felt they were not able to answer some questions accurately, as the tool did not provide options that made sense given their circumstances. This affected participant's confidence that the outcome the tool produced would be relevant to their situation.

'What is the customer role?'

There was widespread confusion over the terminology used in this question. The main areas of concern were who the 'customer' was, and what the term 'engager' meant.

The help page for this question was not considered helpful, as it did not provide definitions of the terminology used. Being unsure of how to answer the first question lowered confidence in the usefulness of the tool, particularly given the warnings on the introduction page about answering accurately.

Worker substitution

Participants found the set of three questions discussing worker substitution confusing and difficult to answer. They were either aware that there was a difference between the questions but unsure of what the difference was and why it was relevant, or they thought the tool might have forced them to answer the same question again:

> *'[T]his is three times the same question. Is there a loop or something that it's not working?'*

> Finance officer, small business, PAYE staff only

One suggested improvement was to make bold or in some way highlight key words if there were similar questions in the tool.

Participants had difficulty in answering the question about what behaviour was contractually obliged. This was particularly the case where the participant was using the tool to categorise a future staff member, as no contract existed yet.

SMEs also raised the point that they might only decide how to handle worker substitution if the situation ever arose.

Questions participants could not reliably answer

Participants were concerned by the following two questions:

'What is the worker's current employment status?'

'How many other engagers has the worker done similar work for during the last 12 months?'

Participants felt that they had no way of knowing the answer to these questions other than asking the member of staff, who might not tell them the truth. Because of this, they would be unable to guarantee an accurate answer to this question. The first question was also considered irrelevant when categorising a future and currently hypothetical employee.

Less relevant questions and questions perceived to lack nuance

Questions were concerning if they appeared to be irrelevant to the SME, or did not offer answers that took account of their circumstances (see case illustration 3.4 below):

'Engager's business' – it was felt there were not enough answer options for this question, and that the overlap in reality between private and public sector was not recognised. These issues were highlighted by participants working in education and distribution.

'Trade of worker' - similarly participants felt that there were not enough options for this question. One participant noted that most businesses would need to select 'other' for this question.

Case Illustration 3.4: ESI questions not relevant to SME's circumstances
Medium size business, with all PAYE staff

The participant, the director of business services, experienced difficulties with a number of questions in the ESI tool, because they did not feel the questions took into account the nature of their work environment, a school.

'… one of the things that's already flagging up in my head at – at this point is this takes no account that I'm in a school… there are lots of controls that are not – nothing to do with employment and everything to do with safeguarding.'

This was a problem for the participant when answering questions about working hours, substitution, and working materials. In the case of substitution the participant pointed out that the question did not allow for the fact that they could not allow people on site that had not passed a security check. However, the participant did find the 'not applicable' option helpful in this particular scenario.

4 Further help and support

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Chapter summary

This chapter explores ways in which HMRC can further help and support SMEs in the classification of employment status. While some feel that the resources already available met their needs, there are a number of suggestions for improvements. These can be grouped into improvements to HMRC's current services, and suggestions for additional services.

Improvements to HMRC's current services
- Simplifying and modernising the website.
- Improving the telephone line.
- Publicising the resources available more widely.

Additional services
- Take steps to clarify the different employment status categories by providing more information, or by altering the categories.
- Pass more responsibility to people who are registered as self-employed.
- Increase enforcement of employment status rules.

The findings in this chapter are based on 33 qualitative in-depth interviews with SMEs.

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4.1 Improvements to current resources

4.1.1 HMRC website, emails and phone line

Some SMEs are happy with the website and feel the information it provides is reasonable. However, the HMRC website is generally viewed as complicated and unwieldy, which in some cases discourages participants from using it. Information is reported to be hard to locate on the website and there are perceived to be too many links to different sources of information. These criticisms were made both of the HMRC website in general, and of the pages relating to employment status. A solution to this is for all of the relevant information to be in one place.

> *'These websites that the government have are too long and very complicated to get to. You go on the main website then you have to put another one in and click on this. It's just - people lose interest.'*
>
> Managing director, micro business, both PAYE and self-employed staff

Suggested improvements to the online ESI Tool are discussed in the section 3.5 on user testing.

A SME who received regular emails from HMRC concerning business help and support suggested these emails could include information and advice about employment status.[13]

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[13] Participant received HMRC emails from the following address:noreply@advice.hmrc.gov.uk

SMEs use the HMRC phone line if they feel uncertain about categorising employment. For one group this was after accessing other information about employment status, which had not provided them with a clear answer. Others found resources such as the HMRC website too complicated and preferred to use the phone line. Those who have used the phone line generally have positive views of it, and feel it helps them in the process of determining employment status. However, a view did emerge that getting through to HMRC on the phone is too difficult.

A number of participants who had not used the HMRC phone line suggested that they would like to be able to call HMRC and speak to someone who could give them a definitive answer for their situation if they were unsure. For some this represented a preference for using a phone line to access assistance. For others a phone line was seen as an additional resource to complement the resources HMRC currently provides.

4.2   Suggestions for additional resources

A number of additional resources were suggested:

- A simple explanation of employment status, and the consequences of miscategorising employees, written in plain English to clarify the basic information for SMEs.

- Examples of what the appropriate employment status would be for different staff in different circumstances to help SMEs understand the regulations in reality.

- A checklist which lists the criteria for different employment statuses for SMEs to refer to when categorising employment.

- Visual resources that allow SMEs to reduce the amount of reading necessary, or provide a substitute for personal interaction. Some participants feel these resources would be more appropriate for them than the blocks of text currently on the websites. Suggestions given were:

  – A flow diagram that allows you to work through an individual's employment status.

  – Videos, webinars, and online training which educate SMEs about what to consider when dealing with employment status.

- Forums that allow employers interact with other employers and to discuss their experiences of categorising employment status. These could occur online, or in person.

A limited awareness of HMRC's information and resources was widespread among SMEs. Some acknowledged that they were unaware of the resources that already existed and therefore felt unable to comment on their effectiveness. However, as described above another pattern that emerged was of SMEs suggesting resources or assistance that already exist, such as a helplines, or tools for determining employment status. This suggests it would helpful for SMEs if HMRC increased awareness of the resources that are already available.

4.2.1 Changes to how employment status is categorised

A number of the suggestions discussed in this section relate to topics discussed in the OTS's 2015 Employment Status Report.[14] Notably, the OTS report stated that a key issue for those dealing with employment status was a lack of certainty and that a main concern

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[14] OTS (2015) Employment Status Report

for businesses was being clear on employment status. This conclusion is supported by the suggestions made by SMEs discussed in this chapter.

Clarification of categories

A recurring theme is that SMEs feel they cannot get a clear and reliable answer on employment status. This makes them feel vulnerable because HMRC or the courts might interpret the situation differently if there was a dispute.

> *'It should be clear-cut. So there's no room for error and there's no - you know, it's black and white. It's either you know you're right or you know you're wrong. You shouldn't have to make a judgement'*
>
>> Managing director, medium sized business, both PAYE and self-employed staff

SMEs with this view also express concerns that they may be caught out by HMRC for making an honest mistake or that the working conditions in their business might be misconstrued to suggest they were incorrectly categorising staff.

One proposed solution to this was for HMRC to provide clearer advice or better resources that give a clear answer on employment status, or some form of guarantee that SMEs are making the right decision. This would enable SMEs to be confident in the decisions they are making.

> *'[J]ust something to say, provided you've given all the information correctly, your - this status will be accepted by HMRC.'*
>
>> Director of business services, medium size business, all PAYE staff

A more radical solution is to alter the different employment categories so that there could not be any ambiguity over employment status. This would remove the need for SMEs to make a judgement, and therefore remove the risk that they had made the wrong decision.

Self-employment: certification and responsibilities

SMEs suggest that it should be possible to check if a potential staff member is actually registered as self-employed. One method suggested for doing this is providing a unique identification number to individuals who are registered as self-employed. SMEs would then be able to check this online or over the phone. Another suggestion was for individuals to be given a certificate if they are self-employed which could be shown to potential employers. These options are thought to help reduce the risk of SMEs employing someone as self-employed who was not actually registered as self-employed or paying tax.

SMEs are also in favour of self-employed staff taking greater responsibility for their own employment status. SMEs suggest providing greater education and guidelines to individuals who register themselves as self-employed to ensure they know whether they are correctly categorised. This would help share the burden of categorisation.

Both of these suggestions were made by SMEs who employed both PAYE and self-employed staff.

Enforcement

One suggestion was to interrogate the data businesses provide to the government for inconsistencies, and increase inspections to ensure that companies are not categorising staff who should be PAYE employees as self-employed. This was felt to be particularly helpful when an organisation has recently changed from paying a lot of staff on PAYE, to not many at all. This suggestion was linked to the view that some businesses were unfairly benefiting from not correctly categorising their staff.

Change the tax regulations which relate to employment status

There were also suggestions about changes that could be made to the tax system that would help SMEs. One participant suggested reducing or even removing corporation tax, as they believed that tax was the reason that employment status mattered to HMRC.

5 Conclusions

The structure of employment within SMEs is varied and differs across different types of business

A quarter of SMEs currently engage self-employed workers. Six per cent only engage self-employed workers and 17% engage both self-employed and PAYE workers. Self-employed workers cover a range of tasks in SMEs, most commonly skilled roles such as construction, electrical and building work, but also professional and administrative roles.

While this type of work is not new to the economy, evidence beyond this research shows that since the start of the twenty-first century the number of people classified as self-employed has risen, and that trend is likely to continue. Further, the digital revolution of recent years makes it easier than ever to find short-term, flexible work.

As such, maintaining a clear understanding of employment practices, and ensuring appropriate tools for the correct classification of staff will be vital.

SMEs use a range of approaches to categorising their staff and have different requirements of classification tools

This research has identified five different models of employment categorisation within SMEs. These are:

- Only employing staff on PAYE terms;
- Offering PAYE terms by default, but considering self-employment if requested or in exceptional circumstances;
- Giving staff a choice over their employment status;
- Making decisions on a case by case basis; and
- Engaging all staff as self-employed by default.

The approaches used are influenced by the type of role that an individual will be performing. It is likely, therefore, that use of these approaches will differ depending on the sector in which the business operates. For instance, this research has shown that some sectors are significantly more likely to offer staff a choice over their employment status (the arts sector and construction in particular), which likely reflects the type of roles on offer. Further, it also shows that some sectors are more likely to face difficulties in classifying their workers – the arts sector, agriculture, and health/social care – and these sectors are typically associated with short-term or ad-hoc work.

Different businesses therefore have different requirements of classification tools. There is not necessarily a one-size-fits-all solution to classification, and a more sector-specific or tailored approach could prove beneficial.

SMEs consider a range of factors when determining the employment status of an individual

When determining the employment status of an individual, SMEs consider a wide range of factors. These include role specific considerations and there is great variation in which characteristics take precedence in decisions. Factors raised consistently in relation to employment status include the length of the contract, the regularity and number of hours worked, autonomy in when and how to work, and the provision of equipment and tools. Also considered are external factors such as the existing

employment status of an individual, risk to the business, administrative burden, the costs associated with operating a PAYE system, and historic or industry-standard practice. The importance that some SMEs place on some of these factors suggests poor understanding and misperceptions of employment status.

In situations where SMEs lack confidence or face specific challenges around categorising, expert advice and risk appear to have a strong influence on decisions, with SMEs often opting to categorise staff as PAYE in order to avoid the risk of miscategorising.

While existing guidance naturally focuses on role specific considerations, it is important to understand other factors that SMEs consider when determining employment status, and help SMEs to understand the relative importance of these factors.

There are two aspects to this. The first is adjusting guidance to incorporate common external factors and advise SMEs on whether or not they are relevant to the process of determining employment status. The second, more long-term challenge, is to take steps to reduce the barriers to correct categorisation, such as the administrative burden of operating a PAYE system, will help SMEs to focus on role specific considerations when determining employment status.

Most SMEs are confident that they are making the correct decisions when determining employment status although confidence does not always correspond with understanding

A large majority of SMEs – 82% – say that they are *very* confident that they are making the correct decisions when classifying staff and a further 15% are *fairly* confident. Indeed, just one per cent of SMEs say that they experience difficulties when classifying employment status. However, the qualitative research shows that confidence (particularly where SMEs have had difficulty categorising due to lack of understanding, lack of experience or ambiguity in roles), is often achieved after SMEs seek information and advice, sometimes resulting in categorising all workers as PAYE to avoid risk.

The qualitative research also indicates that this confidence might not be as strong as SMEs initially suggest, and that it does not always correspond with levels of understanding. When probed, it is clear that not all SMEs are confident of the distinction between employment status categories, or feel that the classification of specific roles is always clear cut. In addition, some SMEs' confidence stems from following industry or historic practice without engaging with or understanding employment status in any depth.

As such, it is important that SMEs are provided with definitions of different employment status categories which are as clear as possible.

Awareness and use of the ESI tool among SMEs is relatively low

A quarter of SMEs are aware of the ESI tool (24%) but just five per cent have used the tool and only two per cent currently use it. Use of the tool does seem to correlate with awareness, and it is most commonly used by medium sized businesses. Those who use the tool are positive about it – most say that it helps them to correctly categorise their staff (79%) and that they would recommend it to other businesses (83%).

This suggests that use of the tool would improve if awareness rises. Raising the profile of the ESI tool among SMEs, particularly among those that have the most difficulty in classification or are exposed to the most risk factors, could increase use.

The ESI tool is being used as an advisory tool, rather than to definitively determine employment status.

Evidence from the qualitative interviews suggests that the ESI tool is not being used to definitively determine employment status. SMEs do not always have sufficient confidence in the outcome of the tool to rely on it alone to provide an authoritative categorisation of employment status for their circumstances. Instead, SMEs use the tool as a guide alongside other sources of information, such as advice from an accountant or lawyer.

The lack of confidence in the outcomes that the tool produces is caused, at least in part, by experience of uncertain results (17% of tool users have experienced this), confusion about the outcomes the tool produces, and concern about perceived ambiguity of some questions and their answer options.

However, the tool does appear to serve a valuable purpose for SMEs. It gives them a process to go through when considering employment status, and provides information about the factors that need to be considered. It also reassures SMEs that they are acting appropriately if it reinforces their existing knowledge or previous decisions.

To improve confidence in the tool, steps could be taken to make the rationale behind outcomes clearer, and refine question wording and answer options to ensure they are easily understood and cover a wider range of possible scenarios. Specific ideas for improvement include:

- Making the link to the tool on the introduction page more obvious.
- Avoiding complicated terminology and ensuring the tool is written in plain English. If terminology or jargon is required, ensure sufficient explanation of any terms.
- Ensuring questions have answers that cover all eventual scenarios. Potentially route users based on their business type so they only answer questions relevant to them.
- Providing more detailed information about why a status was given on the outcome page.

Risk of mis-categorisation is spread evenly across SMEs

This research explored six different 'risk factors': behaviours that could hypothetically increase the risk of mis-categorisation through introducing a subjective element to the decision-making process. These are, in order of prevalence:

- Not currently using the ESI tool;
- Not contacting HMRC staff;
- Not using governmental online guidance;
- Not taking professional advice;
- Taking out insurance to help with costs in the event of an HMRC investigation; and
- Giving staff a choice over their employment status.

On average, SMEs take 2.2 of these risks, with 40% taking more than the average. However, no one group of SMEs appear to be at higher risk than others. Instead, risk appears to be spread evenly across business sizes, employer types and sectors.

Appendix A.   Profile of survey respondents

This appendix sets out the characteristics of businesses taking part in the survey. Unless otherwise stated, all percentages are based on weighted data. All base sizes quoted are unweighted.

Business size

Table 5:1 Business size		
Base: all respondents giving an answer (excluding 84 Don't know responses)	Number (unweighted)	% (weighted)
Total number of workers, excluding owners and partners		
1 to 9 (micro)	668	86%
10 to 24 (small)	598	11%
25 to 249 (medium)	372	2%
Base	1,638	100%

Legal status

Table 5:2 Legal status		
Base: all respondents	Number (unweighted)	% (weighted)
Private limited company, limited by shares (LTD.)	1,120	73%
Sole proprietorship	117	9%
Partnership	142	8%
Private company limited by guarantee	100	3%
Limited liability partnership	28	1%
Public Ltd Company (PLC)	32	1%
A trust	19	*
An unincorporated association	9	*
Private Unlimited Company	8	*
Community Interest Company (CIC, limited by guarantee or shares)	11	*
Industrial and Provident Society	3	*
Friendly Society	6	*
Co-operative	8	*
Other (specified)	76	3%
Don't know	42	1%
Prefer not to answer	1	*
Base	1,722	100%

Years trading

Table 5:3 Years trading		
Base: all respondents	*Number (unweighted)*	*% (weighted)*
Years trading		
Less than one year	12	1%
1 year	27	3%
2 years	37	3%
3 years	63	5%
4 years	69	5%
5 years	53	3%
6 to 10 years	282	22%
11 to 20 years	341	19%
More than 20 years	804	38%
Don't know	34	1%
Base	*1,722*	*100%*

Country and government region of businesses taking part

Table 5:4 Country and government region of businesses taking part in the survey		
Base: all respondents	*Number (unweighted)*	*% (weighted)*
Nation / region of the UK		
Scotland	**365**	**8%**
Wales	**223**	**5%**
Northern Ireland	**196**	**3%**
England	**938**	**84%**
North East	25	3%
North West	120	1%
Yorkshire and The Humber	81	8%
East Midlands	111	8%
West Midlands	89	9%
East of England	128	5%
London	145	21%
South East	148	18%
South West	91	10%
Base	*1,722*	*100%*

This information was taken from the sample file; businesses that were located outside the UK (a very small number located in the Republic Of Ireland but operating also within the UK) were excluded from the analysis.

Industrial classification of businesses taking part

Table 5:5	Industrial classification (SIC2007) of businesses taking part in the survey	
Base: all respondents	Number (unweighted)	% (weighted)
SIC2007 industrial classification		
A - Agriculture, Forestry and Fishing	94	3%
B,D,E - Mining and Quarrying; Electricity, Gas and Air Conditioning Supply; Water Supply	113	1%
C - Manufacturing	160	6%
F - Construction	112	12%
G - Wholesale and Retail Trade; Repair of Motor Vehicles and Motorcycles	146	15%
H - Transportation and Storage	93	4%
I - Accommodation and Food Service Activities	83	6%
J - Information and Communication	85	9%
K - Financial and Insurance Activities	153	2%
L - Real Estate Activities	84	4%
M - Professional, Scientific and Technical Activities	77	13%
N - Administrative and Support Service Activities	77	11%
P - Education	98	2%
Q - Human Health and Social Work Activities	117	5%
R - Arts, Entertainment and Recreation	115	2%
S - Other Service Activities	115	5%
Base	*1,722*	*100%*

Seasonality in employment

Table 5:6	Seasonality in SMEs
Base: respondents from businesses where the number of people working fluctuated across the year.: n = 494	% (weighted)
Thinking about the number of people currently working at [BUSINESS NAME], would you say this is more than normal, less than normal, or about the same as normal?	
More than normal	7%
Less than normal	23%
About the same as normal	70%
Not possible to say [SPONTANEOUS]	*
Base	*100%*

Appendix B. Methodological note

Sampling

A stratified random sample of businesses was drawn from the Inter-Departmental Business Register (IDBR).[15]

To ensure an optimum and efficient sample selection and enable sub-group analysis, the sample was stratified and targets were set for each strata. Specifically, targets were set to ensure a proportionate allocation by Government Office Region and nation, with an equal allocation by SIC category. Further, small and medium-sized businesses were over-sampled. The process for drawing the sample was as follows:

- To begin with, some exclusions from the IDBR were made based on agreed eligibility criteria. Firstly, as it is a survey of SMEs, all those with 250 or more employees were excluded. Secondly, as this is a survey of employers, all those with zero employees were excluded. Finally, SIC sections O (Public administration and defence; compulsory social security); T (Activities of households as employers; undifferentiated goods- and services-producing activities of households for own use); and U (Activities of extraterritorial organisations and bodies) were also excluded. All remaining businesses were considered eligible.
- All eligible workplaces on the IDBR were then divided into strata, based on Government Office Region, 16 high-level industrial sectors based on SIC 2007 and employee size band, using the following classification: micro enterprises (employing 1-9 employees); small enterprises (10-49 employees); and medium-sized enterprises (50 to 249 employees).
- Records were then selected within each of the selection strata using a random start and fixed sampling interval to draw the specified number of records.

Telephone number matching

In total, 10,525 businesses were initially selected. Of these, 82 were removed as being out of scope, leaving 10,443 entries. However, the IDBR does not contain telephone numbers for all entries. Of the initially selected sample, 3,195 SMEs had telephone numbers appended, meaning that 7,248 records (69%) did not have a telephone number.

To address this, NatCen carried out a two-stage telephone number look-up process. Firstly, the entire sample was put through an automated telephone number matching process. This added a further 1,647 telephone numbers. Secondly, all remaining missing telephone numbers were searched for manually. This added a further 2,013 telephone numbers, leaving a final available sample of 6,855, equivalent to 66% of the selected sample.

Appendix table B:1 Telephone number matching		
	N	**%**

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[15] The IDBR covers all businesses registered to pay VAT or that have a PAYE scheme in operation. It is widely regarded as the most comprehensive business sampling frame available, although it does not cover unregistered businesses, so excludes the very smallest non-employing businesses that are not registered for VAT or PAYE.

Appendix table B:1 Telephone number matching		
Total issued from IDBR	10,525	
Excluded (public sector)	82	0.8%
Remaining after exclusions	10,443	
Issued with telephone number	3,195	30.6%
Issued with no telephone number	7,248	69.4%
Telephone number added through telephone matching	1,647	15.8%
Telephone number added through manual search	2,013	19.3%
Final sample with telephone number	6,855	65.6%
Final sample without telephone number	3,588	34.4%

Fieldwork

Fieldwork was conducted by telephone between 12 October and 4 November 2016. As is good practice when trying to maximise response rate on a survey, rather than issue the entire drawn sample, the sample was issued in random batches. In order to reach the target of 1,700 interviews, the sample was uploaded in three batches, totalling 4,960 (the final batch was not required).

From this sample, 646 were found to be deadwood, and therefore ineligible for this research. Of the remaining total of 4,313 eligible contacts, 1,747 interviews were completed. From these, 25 were excluded as employing over 250 staff and therefore being out of scope of the research. Therefore, in total 1,722 interviews were completed at an adjusted response rate of 40%. The table below summarises the outcomes for the issued sample.

Appendix table B:2 Sample outcomes			
Sample outcome		**Response rate**	
Outcome code	**N**	**Unadjusted (%)**	**Adjusted (%)**
Total sample called	4,960		
Total sample eligible	4,314	87%	
Deadwood (ineligible)			
Bad number: fax, modem etc	34	0.7%	
Incorrect number	531	10.7%	
Business no longer operating	4	0.1%	
No reply after max calls	52	1.0%	
Excluded as too large	25	0.5%	
Total ineligible	**646**	**13%**	
Live sample: resolved			
Complete interviews	1,722	34.7%	39.9%
Office refusal	16	0.3%	0.4%
Hard refusal	824	16.6%	19.1%
Respondent ill/away during fieldwork	72	1.5%	1.7%
Live sample: unresolved			
Soft appointment	234	4.7%	5.4%
Call back	1,447	29.2%	33.5%

Weighting

Survey data are weighted. This was done in three stages. Firstly, to correct for the deliberate over-sampling of small and medium sized businesses, and of some SIC categories, selection weights was been calculated. Secondly, to compensate for any bias in the responding sample, a further calibration weight was applied so the final sample matches the profile of SMEs according to region, SIC and employment band. Finally, weights were trimmed to avoid extreme values which would distort the survey data and reduce the reliability of survey estimates.

Appendix C.   Survey questionnaire

Initial contact

ASK ALL

CONT1

Good morning/afternoon/evening my name is .... and I am calling on behalf of HM Revenue and Customs from the National Centre for Social Research.**.**

Cont1a

Can I just confirm that this is [BUSINESS NAME]?

1. Yes [CONTINUE]

2. No

IF Cont1a = No

Cont1Wr

SELECT THE CODE THAT APPLIES

01 "New details given"…..-> enter updated phone number

02 "New details not available"   -> outcome 650

Cont1b

We wrote to your business recently. We are conducting a short piece of telephone research on behalf of HM Revenue & Customs about how businesses classify staff as employees or as self-employed and what HMRC can do to make it easier for businesses.

I need to speak to the person responsible for dealing with employment or staff contracts.

Are you the right person to speak to about this?

1. Yes

2. No

IF CONT1= YES

Cont2

Would it be alright to do a short interview with you now? It will only take around 10 minutes.

IF NECESSARY – **Everything you say will be confidential – no details will be passed back to HM Revenue and Customs and no information will be published that could identify either you or** [BUSINESS NAME].

IF NECESSARY – **You will not have to answer any questions you don't want to. We can always skip a question if you don't want to answer it.**

IF NECESSARY - Businesses have been selected at random to make sure we get a spread of businesses from the different countries and regions of the United Kingdom and a spread of different sizes of SME.

INTERVIEWER: DO NOT READ OUT CODES BELOW

1. Yes – proceed to interview

2. Arrange appointment

3. Refusal to take part – go to RefReas

IF Cont2 = 2 (Arrange appointment)

ContApp

01 "Spoken to NR - soft appointment"…..-> temporary outcome 41

02 "Spoken to NR - hard appointment"…..-> temporary outcome 42

If Cont2 = Refusal…-> outcome 430

RefReas

Could you tell me why you don't want to take part?

INTERVIEWER: DO NOT READ OUT. PROBE

CODE ALL THAT APPLY

1. No time

2. Not interested

3. Don't do surveys

4. Negative mentions of HMRC

5. Don't know enough about employment/contracts

6. Other reasons – PLEASE SPECIFY

7. No response / No reason / Nothing / hung up

If Cont1 = NO

Cont3

Can you give me the name of the person who would deal with employment and staff contracts at [BUSINESS NAME]**?**

1. Yes – details provided

2. No – details refused

3. Don't know – arrange to call another time

IF CONT3 = YES

ContDetN

What is the name of the person responsible for staff contracts and employment at [BUSINESS NAME]**?**

Enter name or select DK / REF

IF CONT3 = YES

ContDetP

And what is the position or job title of {textfill name from ContDetN or "the person I should call"}**?**

Enter job title/position

IF CONT3 = YES

ContDetT

And is [BUSINESS TEL NO] **the best number to call?**

1. Yes

2. No

IF ContDetT=NO

ContDetT2

Can you tell me what number would be best to use to call {text fill from ContDetN or ContDetP}**?**

Enter full number including STD code and any extension or select DK / Ref

IF Cont3 = NO

Cont4

Can you tell me the job title of the person we should ask for when we call back?

ENTER JOB TITLE

_____

REF

ADD

Requests for copy of letter to be sent by email/post

Business information

ASK ALL

LegStat

Firstly, could you tell me the legal status of the business?

READ OUT AS NECESSARY. ALLOW MULTICODE ONLY IF 'OTHER' MENTIONED

INTERVIEWER NOTE: IF BUSINESS NAME CONTAINS 'LTD' OR 'LIMITED' THEY ARE USUALLY A LIMITED. COMPANY (CODE 2).

IF 'PRIVATE LIMITED COMPANY' MENTIONED, CHECK WHETHER LIMITED BY SHARES OR BY GUARANTEE.

FOR OTHERS RECORD ALL INFORMATION VERBATIM TO ESTABLISH OWNERSHIP. N.B. "CHARITY" IS NOT A LEGAL STATUS)

1. Sole proprietorship

2. Private limited company, limited by shares (LTD.)

3. Public Ltd Company (PLC)

4. Partnership

5. Limited liability partnership

6. Private company limited by guarantee

7. Community Interest Company (CIC, limited by guarantee or shares)

8. Friendly Society

9. A Co-operative

10. Industrial and Provident Society

11. Private Unlimited Company

12. Foreign Company

13. A trust

14. An unincorporated association

15. Other (SPECIFY)

Don't know

Refused

ASK ALL

YrsTrad

And how many years has this firm been trading? This includes under all ownerships and all legal statuses.

SINGLE-CODE

IF NEEDED: **If you don't know exactly, please give a rough estimate**

PROMPT IF NECESSARY.

1. Less than one year

2. 1 year

3. 2 years

4. 3 years

5. 4 years

6. 5 years

7. 6 – 10 years

8. 11 – 20 years

9. More than 20 years

Don't know

Screening questions

ScrInt

I'd now like to ask you some questions about the workforce at [BUSINESS NAME].

ASK ALL

NumStaff

Thinking about all the people who currently work at [BUSINESS NAME]**… How many people currently work at your business across all sites, excluding owners and partners?**

IF NEEDED: If you don't have the exact figure to hand, please give an estimate for the current month.

READ OUT:

- INCLUDE FULL AND PART TIME

- INCLUDE TEMPORARIES/CASUALS,AND INCLUDE AGENCY STAFF

- INCLUDE SELF-EMPLOYED

- EXCLUDE OWNERS/PARTNERS, BUT OTHER DIRECTORS COUNT AS EMPLOYEES

ENTER NUMBER (RANGE=0-99,999)_____

DK

ASK ALL

StfTypP

Still thinking about the people who currently work at [BUSINESS NAME] **are any of your staff…**

… employed on a PAYE basis?

1. Yes

2. No

DK

INCLUDE TEMPORARIES/CASUALS TAKEN ON AS PAYE EMPLOYEES, BUT NOT AGENCY STAFF

DO NOT INCLUDE SELF-EMPLOYED

EXCLUDE OWNERS/PARTNERS, BUT OTHER DIRECTORS COUNT AS EMPLOYEES

ASK IF StfTypP=YES

StfTypPN

How many individuals currently work <u>as PAYE employees</u> at your business across all sites, excluding owners and partners?

IF NEEDED: **If you don't have the exact figure to hand, please give an estimate for the current month.**

INCLUDE FULL AND PART TIME

INCLUDE TEMPORARIES/CASUALS WHO ARE PAYE EMPLOYEES BUT EXCLUDE AGENCY STAFF

EXCLUDE SELF-EMPLOYED

EXCLUDE OWNERS/PARTNERS, BUT OTHER DIRECTORS COUNT AS EMPLOYEES

ENTER NUMBER (RANGE=0-99,999)_____

DK

NumStDUM

CATI TO CODE AUTOMATICALLY FROM StfTypPN TO FOLLOWING BANDS FOR MONITORING QUOTAS:

QUOTAS

1. 1-9 employees (Micro)

2. 10-49 employees (Small)

3. 50-249 employees (Medium)

ASK ALL

StfTypSE

And are any of your staff currently classified as <u>self-employed</u>? That is, not as employees on a PAYE basis?

1. Yes

2. No

DK

INTERVIEWER – READ OUT:

- PLEASE INCLUDE TEMPORARIES/CASUALS WHO ARE TAKEN ON AS SELF EMPLOYED,

- DO NOT INCLUDE AGENCY STAFF

- DO NOT INCLUDE STAFF WHO ARE PAYE EMPLOYEES

- EXCLUDE OWNERS/PARTNERS AND OTHER DIRECTORS

ASK IF StfTypSE=YES

StfTypSN

How many workers does [BUSINESS NAME] **currently have who are self-employed?**

IF NEEDED: If you don't have the exact figure to hand, please give an estimate for the current month.

INCLUDE FULL AND PART TIME

INCLUDE TEMPORARIES/CASUALS WHO ARE TAKEN ON AS SELF EMPLOYED, BUT NOT AGENCY STAFF

DO NOT INCLUDE STAFF WHO ARE PAYE EMPLOYEES

EXCLUDE OWNERS/PARTNERS AND OTHER DIRECTORS

ENTER NUMBER (RANGE=0-99,999)_____

DK

ASK ALL

StfTypAg

Does [BUSINESS NAME] **take on individuals <u>through agencies</u>? That is, not as employees on a PAYE basis, nor as self-employed.**

1. Yes

2. No

DK

INCLUDE AGENCY STAFF WHETHER THESE ARE TAKEN ON AS TEMPORARY/CASUAL STAFF OR ON A LONGER TERM BASIS.

THE KEY ISSUE IS THAT THESE INDIVIDUALS HAVE AN EMPLOYMENT CONTRACT WITH THE <u>AGENCY</u> THAT SUPPLIES THEM AND NOT WITH THE BUSINESS WHERE THEY ACTUALLY WORK.

DO NOT INCLUDE STAFF WHO ARE PAYE EMPLOYEES.

DO NOT INCLUDE SELF-EMPLOYED STAFF.

EXCLUDE OWNERS/PARTNERS AND OTHER DIRECTORS

ASK IF StfTypAg=YES

StfTypAgN

How many individuals does [BUSINESS NAME] **currently have who are supplied by an agency?**

IF NEEDED: If you don't have the exact figure to hand, please give an estimate for the current month.

INCLUDE AGENCY STAFF

EXCLUDE ALL INDIVIDUALS WHO ARE EMPLOYEES ON A PAYE BASIS

EXCLUDE TEMPORARIES/CASUALS TAKEN ON AS PAYE EMPLOYEES

EXCLUDE SELF-EMPLOYED

EXCLUDE OWNERS/PARTNERS AND OTHER DIRECTORS

INCLUDE FULL AND PART TIME

ENTER NUMBER (RANGE=0-99,999)_____

DK

Seas

Does the number of people working at [BUSINESS NAME] **vary across the year?**

IF NEEDED – **This is sometimes called seasonal variation or seasonality. For example, you might take on extra people during the holidays or over Christmas and New Year.**

1. Yes

2. No

DK

SeasHiLo

Thinking about the number of people <u>currently</u> working at [BUSINESS NAME]**, would you say this is more than normal, less than normal, or about the same as normal?**

1. More

2. Less

3. About the same

4. SPONTANEOUS ONLY – Not possible to say / can't say

ASK IF StfTypSE=YES

Thinking now about your self-employed staff…

QSETyp.

Does your business take on self-employed people at any of the following levels or roles? Please answer Yes or No to each type.

READ OUT. CODE ALL THAT APPLY

1. Yes

2. No

DK

QSETyp1

Managers, Directors or Senior Officials

READ OUT IF NECESSARY: These are roles associated with the efficient functioning of organisations and businesses

QSETyp2

Professional staff

READ OUT IF NECESSARY: These are roles that require a degree or equivalent qualification

QSETyp3

Associate professionals or technical staff

READ OUT IF NECESSARY: These are roles that require a high-level vocational qualification or equivalent experience

QSETyp4

Skilled tradespeople

READ OUT IF NECESSARY: These people would do work that requires a large amount of training or specialist skills

QSETyp5

Administrative or secretarial staff

READ OUT IF NECESSARY: This would involve office work that requires a good standard of general education

QSETyp6

Sales and customer service

QSETyp7

In Elementary occupations

READ OUT IF NECESSARY: This would include occupations that require knowledge and experience to perform routine tasks. They do not usually require formal qualifications but experience-related training.

StTypDum

CREATE DUMMY VARIABLE BASED ON **StfTypP, StfTypAg** and **StfTypSE**

1. PAYE only and no self-employed (StfTypP=Yes and StfTypSE = No/DK)

2. Self-employed and no PAYE (StfTypP = No/DK and StfTypSE = Yes)

3. Both PAYE and self-employed (StfTypP = Yes AND StfTypSE = Yes)

4. Employment status not known (StfTypP = DK AND StfTypSE = DK)

Classifying individuals

We are interested in how businesses classify the status of their workers, such as whether they are PAYE or self-employed.

1.

ASK ALL

StClDif

Does your business ever have any difficulties in deciding whether an employee should be classified as PAYE or self-employed?

Please include any difficulties you have face in classifying employees, including if you have carried out this process on behalf of a client.

1. Yes

2. No

3. DK

ASK ALL WITH MORE THAN 0 EMPLOYEES (IF NUMSTAFF = MORE THAN 1)

CatDoInt

Does your business do any of the following things when categorising people as either PAYE employees or self-employed…

PROGRAMMER - RANDOMISE STATEMENTS CAtDo1 to CatDo5. And put on one screen if possible.

CatDo1

[Does your business…]

Use guidance on the HMRC or GOV.UK websites?

1. Yes

2. No

3. DK

CatDo2

[Does your business…]

Contact HMRC staff, either by phone, email, letter or in person?

1. Yes

2. No

3. DK

CatDo3

[Does your business…]

Take advice from an accountant, lawyer or legal advisor whether inside or outside the business?

1. Yes

2. No

3. DK

CatDo4

Take out insurance to help with costs in the event of an HMRC investigation?

Yes

No

DK

CatDo5

[Does your business…]

Use agencies to provide staff in order to avoid [BUSINESS NAME] **having to categorise staff itself as either PAYE employees or self-employed?**

1. Yes

2. No

3. DK

CatDo6

Does [BUSINESS NAME] **ever offer staff a choice between joining as a PAYE employee or being self-employed?**

IF NECESSARY: **Please think about the last 12 months**

1. Yes

2. No

DK

ASK IF CATDO6 = YES

CatDoOft

How often would you say that [BUSINESS NAME] **offers staff a choice between joining as a PAYE employee or being self-employed?**

1. Always
2. Sometimes
3. Hardly ever
4. Never

DK

Employment Status Indicator

ASK ALL

ESIAw1

Have you ever heard of HMRC's Employment Status Indicator tool – the ESI? It doesn't matter whether you have actually used it.

1. Yes

2. No

3. DK / Not Sure

IF ESIAw = No or DK or Not sure

ESIAw2

READ OUT

The Employment Status Indicator is an online tool to help businesses decide whether workers should be classified as self-employed or allocated to PAYE. The tool asks the user some questions about the nature of the worker's employment and responsibilities and, based on the answers to those questions, tells the user whether the worker is self-employed or a PAYE employee.

Now that you have heard that description, is the Employment Status Indicator something that you had heard of previously? It doesn't matter if you have never used it.

1. Yes

2. No

_

3. DK / Not sure

IF ESIAw1 = Yes OR ESIAw2 = Yes

ESIUsEv

Have you ever used the HMRC Employment Status Indicator tool at [BUSINESS NAME] **or at a previous business?**

1. Yes, at this current business only

2. Yes, at this current business and at a previous business

3. Yes, at a previous business only – not at this current business

4. No, have not used the ESI tool

DK

ESIUsDum

CREATE DUMMY VARIABLE

1. Has used ESI (If ESIUsEv = YES 1, 2, 3)

2. Has not used ESI (If ESIUsEv = NO = 4)

3. Unclear whether used ESI (If ESIUsEv = DK)

IF ESIUsEv = NO

ESIUsNev

Why have you never used the HMRC Employment Status Indicator tool at [BUSINESS NAME]**?**

OPEN QUESTION. CODE TO LIST BELOW AND TYPE IN VERBATIM FOR OTHER OPTIONS MENTIONED

We use an accountantWe only employ people on a PAYE basis

Never had need/Always know how to classify

No reason

No staff/not applicable

DK

IF ESIUsEv = YES

ESIUsNw

Does your business currently use the Employment Status Indicator tool?

1. Yes, usually/always

2. Yes, sometimes

3. No

IF ESIUsNW = 1 OR 2

ESIUsNw1

When you use the Employment Status Indicator tool, is this on behalf of your own business, for another business, or both?

1. Own business

2. Other business

3. Both

ASK IF ESIUsNw = 1 or 2

ESIUComp

Do you believe that using the ESI tool is compulsory for not compulsory?

1. Compulsory

2. Not compulsory

3. Don't know

ASK IF ESIUsNw = 2 or 3

ESIUsNot

Can you say why your business does not use the Employment Status Indicator tool [*IF ESIUsNw=2* more often]?

INTERVIEWER: CODE MENTIONS OF RESPONSES BELOW AND ADD ANY ADDITIONAL ISSUES UNDER OTHER/SPECIFY.

PROBE AS NECESSARY BUT DO NOT PROMPT. DO NOT READ OUT CODES

1. Not confident about using the ESI tool

2. ESI tool answers are not reliable

3. ESI tool gives outcomes where it is not clear whether a person should be PAYE or self employed

4. Difficult to understand the ESI tool questions

5. Difficult to understand the ESI tool outputs / results

6. Previous experiences of challenges to ESI results by HMRC or by workers

7. Just don't like the ESI tool

8. Use an alternative process for determining employment status

9. Other – specify

DK

ASK IF ESIUsDum = 1 (Yes)

ESIEasCl

Now thinking about your experience of using the Employment Status Indicator tool to decide whether to classify workers as PAYE employees or self-employed…

To what extent would you say that the Employment Status Indicator tool makes it easier or more difficult for your business to make the right decisions when classifying workers – would you say the ESI tool…

1. Makes it much easier to make the right decisions about employment status

2. Makes it somewhat easier

3. Makes it somewhat more difficult

4. Makes it much more difficult to make the right decisions about employment status?

DK

ESIEasUs

How easy or difficult do you find using the ESI tool? Do you find it…

1. Very easy

2. Fairly easy

3. Fairly difficult

4. Very difficult

5. SPONTANEOUS ONLY – it depends

DK

ESIEasQn

How easy or difficult do you find it to understand the <u>questions</u> in the ESI tool? Do you find the questions…

1. Very easy to understand

2. Fairly easy to understand

3. Fairly difficult to understand

4. Very difficult to understand

5. SPONTANEOUS ONLY – it depends

DK

ESIEasRs

And when you get the results from the Employment Status Indicator tool, do you understand why the tool has given a particular result? Would you say you…

1. Always understand the reasons for a particular result

2. Sometimes understand the reasons for a particular result

3. Rarely understand the reasons for a particular result

4. Never understand the reasons for a particular result?

5. SPONTANEOUS ONLY – it depends

DK

ESIEasCnf

When you get the results from the Employment Status Indicator tool, how confident, if at all, are you that the tool is giving the correct decision in categorising an individual as an employee or as self-employed – would you say you are…

1. Very confident

2. Fairly confident

3. Not very confident

4. Not at all confident

5. SPONTANEOUS ONLY – it depends

DK

ESIUnc

Have you ever used the HMRC Employment Status Indicator tool and had an uncertain result, that is, where the ESI tool output says that it is not possible to determine whether a person should be categorised as an employee or as self-employed? This can be for your own business, or on behalf of another business.

1. Yes

2. No

DK

ASK IF ESIUnc = 1

ESIUncWh

What have you done in that situation?

IF NEEDED: WHERE YOU USED THE HMRC EMPLOYMENT STATUS INDICATOR TOOL AND IT GAVE AN UNCERTAIN RESULT THAT, THAT IS, WHERE THE ESI TOOL OUTPUT SAYS THAT IT WAS NOT POSSIBLE TO DETERMINE WHETHER A PERSON SHOULD BE CATEGORISED AS AN EMPLOYEE OR AS SELF-EMPLOYED

OPEN QUESTION – TYPE IN VERBATIM

INTERVIEWER: CODE MENTIONS OF RESPONSES BELOW AND ADD ANY ADDITIONAL ISSUES UNDER OTHER/SPECIFY.

PROBE AS NECESSARY BUT DO NOT PROMPT. DO NOT READ OUT CODES

1. Always/usually categorise the person as a PAYE employee

2. Always/usually categorise the person as self-employed

3. Don't employ the person

4. Go through an agency instead

5. Take advice from HR / legal advice / accountant advice

6. It depends

7. Other - specify

DK

ASK ALL

ESIRec

How likely, if at all, is it that you would recommend the HMRC Employment Status Indicator tool to other businesses like yours?

1. Very likely

2. Fairly likely

3. Not very likely

4. Not at all likely

ESIRecUn

Why would you be unlikely to recommend the ESI tool to other businesses like yours?

INTERVIEWER: CODE MENTIONS OF RESPONSES BELOW AND ADD ANY ADDITIONAL ISSUES UNDER OTHER/SPECIFY.

PROBE AS NECESSARY BUT DO NOT PROMPT. DO NOT READ OUT CODES

1. Difficult to use

2. Unreliable outcomes

3. Not confident in the results

4. Other - specify

DK

ESI Imp

What improvements, if any, would you like to see to the HMRC Employment Status Indicator tool?

INTERVIEWER: CODE MENTIONS OF RESPONSES BELOW AND ADD ANY ADDITIONAL ISSUES UNDER OTHER/SPECIFY.

PROBE AS NECESSARY BUT DO NOT PROMPT. DO NOT READ OUT CODES

1. Simplified question wording

2. Improved guidance

3. Online or telephone helpline for advice

4. Clear outcomes

5. Other - specify

DK

ESConf

Regardless of whether you use the HMRC Employment Status Indicator tool, how confident, if at all, are you that your business is making the correct decisions in assigning staff as PAYE employees or as self-employed? Would you say you feel…

1. Very confident

2. Fairly confident

3. Not very confident

4. Not at all confident

ASK ALL

AnyElse

Is there anything else you would like to tell us about your experience of allocating workers to PAYE employee status or to Self-employed status?

OPEN QUESTION. TYPE VERBATIM. PROBE

ASK ALL

FollowUp

As part of this study for HM Revenue and Customs, the National Centre for Social Research is carrying out further research with businesses to try to understand the process of allocating staff to self-employed status or to PAYE employee status. Are you happy to be recontacted in relation to a further interview?

1. Yes

2. No

DK

IF FollowUp=DK OR NO

Thank and close

ASK IF FOLLOWUP = Yes

QualConts

Take details for Qual follow-up

Name

Position/Job title

Telephone number

Email

Address

ESITool

If don't know the ESI Tool, offer to give them the website address.

Thank and close

Appendix D. Interview topic guide

Research aims:

- Gain an in-depth understanding of the reasons for mis-categorisation by SMEs directly engaging workers

- Understand what support is needed to reduce mis-categorisations by SMEs, including improvements to the ESI online tool

Overview of topics to be covered in interviews:

- Process of determining employment status of employees

- Reasons for potentially mis-categorising employment status

- Issues experienced and support received

- Use and views of the ESI tool

How to use this topic guide:

- This document is a guide to the principal themes and issues to be covered

- Fully formed questions are avoided to ensure researchers are responsive and flexible in their questioning

- Probes such as 'why', 'how' etc are not included in the guide. These are asked by researchers as and when appropriate

- This strand is concerned with SMEs who directly engage workers, clarify that agency workers are excluded

1   Introduction

- Introduction to researcher. Thank you for agreeing to take part

- Introduction to NatCen – independent research organisation, commissioned by HMRC to carry out this study

- Explanation of research:

    – Explores barriers small and medium sized businesses face classifying staff as employees or self-employed

    – During the survey you mentioned some challenges in determining staff employment status. We would like to explore these issues in more detail during this interview

    – We want to talk to you about your experiences of determining employment status and how you think HMRC can make it easier for businesses to classify staff correctly

- Participation is voluntary – there are no right or wrong answers, you can choose not to discuss any issue

- What you say is confidential. We will write a report of our findings but no names of businesses or individual participants will be included. You will not be identifiable to anyone else in the report

- NatCen will not pass any information on to HMRC about the businesses that have taken part in the research. Nothing you say in this interview will affect your future dealings with HMRC

- We will be recording the interview so we have an accurate record of what is said
  - Recorder is encrypted and files stored securely in line with Data Protection Act 1998
  - Only the research team will have access to the recordings

- The interview will last 45 minutes (if on the telephone) and one hour (if face-to-face)

- Questions?

- Ask for permission to start recording

2 Background information about participant and SME

Section aim: to 'warm up' participant and gather contextual information about the participant and SME.

- About the **participant**
  - Role within the business
  - Length of time within the business
  - Role and responsibilities in relation to categorising employment
    - Length of time doing this role

- About the **business,** *ask participant to briefly describe:*
  - Purpose of the business
  - How long it has been trading for
  - Who it was set up by
  - Where is business based
  - Occupational profile of the business:

Re-cap information given in survey:		*Use the following probes for each category:*
Total number of employees	…….	• Whether number of workers is still correct and up to date
Full time staff	…….	• Types of role performed in this category of staff
Part time staff	…….	• If and how varies throughout the year (e.g. seasonally), why
Self-employed staff	…….	
Agency workers	…….	
Employed on PAYE basis	…….	

3   Process of determining employment status

Section aim: to get an overview of the way businesses categorise employment status.

- How SME determines employment status of workers (*if necessary prompt participant to reflect back on the last time they had to determine employment status and the process they* went *through*)

    - Who involved apart from themselves, how involved (*some businesses may seek advice from someone else or offer staff a choice*)

    - Stages involved, what they do / consider first, next, after that…

    - Factors considered:

        - **Distinction between employed and self-employed** (*probe around characteristics that spring to mind when thinking about 'employees' at their business and how this differs to people who are 'self-employed' at their business*)

        - Whether any **confusion or overlap** in definitions (*ask to refer back to own workforce, explain will ask in more detail about this later*)

        - Administrative burden / red tape as a factor considered when categorising employees

        - Tax or other costs to the business, or worker (*probe on the specific taxes they are referring to, which other costs they consider and in what circumstances they are considered*)

        - Other

> *Prompts*
>
> - *Whether employee obliged to carry work out personally*
> - *Extent of autonomy of how, where and when work is undertaken*
> - *Extent required to make use of own equipment*
> - *Skills or expertise of worker*

- What **informs the process** / decision including information, advice or resources used (*survey responses will indicate what has been used*)

    - Reasons for accessing or not accessing these sources

    - Experience of information, advice or resources

> *Prompts*
>
> - *Guidance on HMRC or GOV.UK websites*
> - *Contact with HMRC staff*
> - *ESI tool*
> - *Advice from lawyer / legal advisor*
> - *Advice from accountant / financial advisor*
> - *Advice from employment agency*

- - Helpfulness

  - Clarity

  - Relevance

  - Ease of access

- **Alternative ways of determining employment status used** in the past, reasons for variation

- **Overall experience** of determining employment status

  - How long it takes

  - How resource intensive

  - Positive experiences

  - Negative experiences

  - Challenges experienced

4   Challenges experienced and support received

Section aim: explore specific examples of challenges categorising staff and any support accessed to help resolve the issue, and how useful it was.

- Ask participant to **describe a situation/s** when it has been difficult to determine whether a worker is employed or self-employed

  - What was difficult about the process

  - What did they do

    - Any information / advice / support sought

    - Reasons for accessing / not accessing support/guidance

    - Views on support/guidance received, whether it provided the answers needed

  - How situation resolved

- **Implications** of determining employment status incorrectly, any direct experience of this

- (*If not already discussed*) If participant has said they are 'not very confident' or 'not at all confident' about their decisions in categorising staff

  - Reasons for their lack of confidence

  - Workers / types of workers does this relates to

  - Areas of confusion

  - Whether information / advice / support sought and received

  - Helpfulness of this information / advice / support

5 Experience of ESI tool (those aware of tool only)

Section aim: to capture views of the ESI tool amongst those who have used it and further explore facilitators and barriers to its use.

Note to interviewer: survey responses will indicate awareness and use of tool, as well as other views and experiences of the tool

- For SMEs who **use or have used the ESI tool** (*for each topic listed, ask openly and then probe on survey responses to the Employment Status Indicator section of the questionnaire if not raised spontaneously*)

    - Reasons for using the ESI tool
    - General experience of using
        - Accessibility, how easy to find
        - User friendliness
            - Ease of understanding questions
            - Ease of understanding outcome
        - IT or technical issues
        - General helpfulness in decision-making around classifying workers
        - Outcome, and views of / confidence in outcome (*probe around uncertain results*)
        - Any issues / challenges
        - Use of user manual
            - If yes, how helpful
            - Improvements needed

- For SMEs who have **heard of but never used the ESI tool**

    - Reasons for not using the ESI tool (*ask openly and then probe on survey responses to **ESIUsNot** if they are not raised spontaneously*)
        - Accessibility
        - Time
        - Trust / confidence
        - Other barriers to use

- Views on **future use ESI tool**

    - Used: Whether they would use it again
    - Not used: What would encourage them to use it in future

- Whether they would **recommend** it to others, reasons for and against (*probe on survey response to **ESIREC***)

- Awareness and views of **other support / advice available** (*ask for examples*)

6   Suggestions for support and concluding thoughts

- Reflections on the definitions of PAYE employee and self-employed
- *(If 'worker' category is raised as a source of confusion)*
    - Particular issues of confusion, why
    - Any examples
- Overall how easy / difficult to determine employment status of staff
- Help that would be useful to categorise correctly
    - How this help should be available /delivered, who by
    - Whether their business would use this type of support
- How current, advice, guidance and tools could be improved
- What else HMRC can do to support SMEs
- View on importance of reducing mis-categorisation

Check if anything else to add, thank and close

- Ask whether participant would consent to interview transcript being shared with HMRC. Explain that
    - This is entirely voluntary
    - Transcripts will be fully anonymised (we will remove any information that identifies individuals and businesses)
    - We would be happy to send them the transcript before it goes to HMRC
    - Seeing transcripts helps HMRC to quality assure our work
- Please record participants consent to send anonymised transcript to HMRC
- Anything else
- Questions

Appendix E.   User testing script

Introduction

- The aim of this section of the interview is to explore your experiences of using the tool. We would you like about the tool and what you think could be improved. By doing this we can help make sure that the ESI tool is as clear as possible for people who use it in the future.

- In a moment we will ask you to use the tool thinking about the person you most recently categorised employment status for.

- I would like to watch you using the tool and then I will ask you some questions about how easy or difficult you found the process.

- This is not a test. If you have any difficulties at all using the tool, or find something unclear, please let me know. If you have problems then other people will as well.

- Can I just check, did you look at the ESI tool in advance of the interview?

7   Think-aloud training

NOTE TO INTERVIEWER:

- Explain that you are about to ask the participant to use the ESI tool.

- Whilst they fill this in you want to know their impressions of the tool, what they are looking at and what they are thinking about.

- Explain the 'Think Aloud' technique using the windows example

> **Windows example:** I would like you to have a practice at 'thinking aloud.' I am going to ask you a question and I want you to tell me what you are thinking as you work out your answer…
>
> 'How many windows are there in your home?' Please describe what you are thinking as they work out your answer….

- Encourage think aloud whilst completing the process…

8   Scenario: Using the ESI tool

Section aim: To get participants' initial feedback on the ESI tool and the sections/questions (if any) they found difficult to answer

- Ask the participant to go onto the ESI tool page and start filling it in based on a worker for whom they experienced confusion or difficulty categorizing.

NOTE TO INTERVIEWER: Please allow participants to find to find the tool themselves but if they struggle point them to the page. If needed the address of the tool is: http://tools.hmrc.gov.uk/esi/investigate/ESI/en-

GB/Attribute~complete~global~global/qs%24s38%40Interviews_screens_xint%24glob
al%24global?user=guest

Observations
NOTE TO INTERVIEWER: Please note whilst observing:

Observations- please circle

- **Did the participant find the page easily?**   YES NO
- **Did the participant read all of the instructions?**   YES NO
- **Did the participant open up the further guidance?**   YES NO
- **Did the participant open up any of the help pages?**   YES NO
- **Did the participant hesitate at any of the questions?**   YES NO
- **IF YES- Which questions did they hesitate at?**

……

……

General probes – to be asked after completion of the tool

NOTE TO INTERVIEWER: Some probes may have been covered during think aloud.
Please check if anything has been missed and use spontaneous probes to cover
situations not pre-empted where appropriate.

- Explain you are now going to explore with them how they found using the tool
    - How did you find the process?
    - How easy or difficult did you find using the tool to categorise employment
      status?
    - How confident do you feel about the outcome you were given by the ESI
      tool?
    - Were there any questions where you were unsure of what was being
      asked? IF YES WHICH?
    - Were there any questions where you were unsure of your answer? IF YES
      WHICH?
    - IF USED THE TOOL PREVIOUSLY
    - In the past when using the tool have you ever been unsure of your answer
      to any of the questions? IF YES WHICH?
    - How useful do you find the ESI tool is in identifying employment status?

9   ESI Tool introduction

Section aim: to understand if participants read and understand the introduction text.

- Suggested probes
    - What did you think of the introduction page?
    - Did you read all of the text on the introduction page?
    - Did you find anything unclear in the introduction? IF YES WHAT?

10   Exploring specific questions

Section aim: to explore how easy or difficult participants found answering specific questions and how they decided on their answers

- Suggested probes

    - How easy or difficult did you find answering the following questions:

    - What is the customer role?

    - What is the worker's current employment status?

    - INT ASK THESE PROBES FOR ANY QUESTIONS R SAID THEY HAD DIFFICULTY WITH

    - How did you decide on your answer to this question?

    - Is there anything about these questions you don't understand?

    - What did you think of the output page?

    - Was there anything you found difficult to understand on the outcome page or was everything clear?

11   Layout

Section aim: to get top-level information on what participants thought about the layout of the tool.

- Suggested probes

    - What did you think of the layout of the ESI tool?

    - Did you notice the help buttons available? Are these helpful?

    - What would you do if you had any problems using the tool?

    - Do you have any suggestions on how this tool could be improved?

        - Question wording

        - Question phrasing

        - Layout