



GOING IT ALONE, MOVING ON UP: SUPPORTING SELF-EMPLOYMENT IN THE UK

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SELF-EMPLOYMENT IN THE UK

Benefits of self-employment*



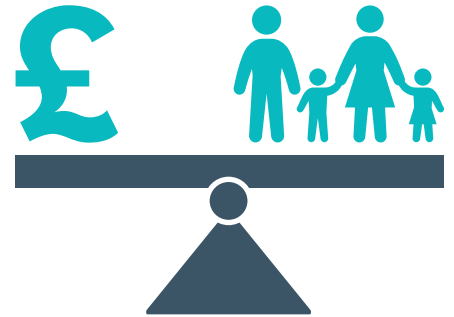
51%

Opportunity to fulfil a personal vision



79%

Independence at work



61%

Better work/life balance

Access to financial products



21%

report difficulties accessing a mortgage

Challenges of self-employment



44%

lack of certainty of earnings**

Savings and pensions



31%

are saving into a private pension

Ambitions for the future



60% plan to remain self-employed/running the same business in five years

Training and business support



have taken advantage of government-backed schemes providing business advice or support in the last five years

* Percentage of members who ranked these options in their top three benefits associated with self-employment.

** Percentage of members who ranked this as one of the top three challenges of being self-employed

FOREWORD

Championing the self-employed is in our DNA. To quote our full title – the ‘National Federation of Self-Employed and Small Businesses’ – we exist to promote and protect the interests of all those who set up their own businesses and are self-employed. Since we were established in 1974, we have worked hard to ensure society recognises, values and adequately rewards the endeavours of those who are self-employed. While the average FSB member who employs people has seven staff, nearly a quarter go it alone. We therefore remain the leading champion of the self-employed and smaller firms.

This report shows that more people are taking the brave decision to become their own boss than ever before. It also shows that the value of self-employment is now more widely recognised by policymakers than ever before. With 5.4 million businesses operating in the UK today, of whom four million are going it alone, it is clear that the self-employed represent the engine room of the economy – the hidden heroes that generate growth and wealth throughout the country. The Government and opposition parties have rightly pledged to support this enterprising spirit and make it easier for more people to set up the businesses of the future but there is a lot more that can be done.

Our report contains a series of recommendations to Government on how best to support the self-employed. It also recognises that self-employment isn’t easy and often comes with many challenges. We shed light on some of the personal challenges facing the individuals behind many of these businesses, including the lack of secure income and the difficulties of saving for retirement, obtaining a mortgage and taking time off to have a family.

We hope the ideas contained in this report will prove useful for those seeking to develop solutions to these problems – ideas which FSB is committed to taking forward, to support the millions in the UK today who ‘go it alone’ and help them to ‘move on up’.



Martin McTague
Policy Director

EXECUTIVE SUMMARY

Since the recession, the number of people in self-employment in the UK has grown significantly and now stands at the highest level in 40 years. More and more people are going it alone regardless of their circumstances. Setting up a business has never been easier, aided by new technology and commercial web platforms, which are helping to widen access to entrepreneurship.

The growth in self-employment does not appear to be simply a cyclical phenomenon; rather it amounts to a structural re-shaping of the economy and labour market that began in the early 1980s and, after a short period where self-employment flat-lined and fell in the 1990s, re-emerged in the early 2000s. Today approximately 15 per cent of the workforce is self-employed, up from 12 per cent in 2000 and eight per cent in 1980¹.

Faced with this fact, the self-employed have received growing interest in academic and policy circles in recent years. Government too has recognised the need for public policy to adapt to reflect the rise in the number of people going it alone – both in regards to business policy, but other aspects of policymaking including the social security net, savings and childcare. Prior to the 2015 election, the Conservative Party pledged in its manifesto to introduce measures to address disadvantages facing the self-employed and commissioned two independent reports, by Julie Deane OBE² and Baroness Michelle Mone OBE³ into self-employment, which were published earlier this year. Similarly, the Labour Party has under Ed Miliband and now Jeremy Corbyn set out plans to support those that go it alone. Supporting the self-employed has never before received as much interest among policymakers.

The aim of this report is twofold: firstly, to provide further evidence on the characteristics, motivations and concerns of the UK's army of self-employed workers, and second, to make a series of practical policy recommendations for Government to support the self-employed. Our findings are centred on new survey data, published here for the first time, which set out new perspectives on self-employment and what more can be done to support the smallest of entrepreneurs. However, rather than focusing exclusively on measures to support the self-employed grow their business – an area that is natural territory for FSB – our recommendations instead focus on the 'personal side' of self-employment and seek to address the more personal challenges experienced by many self-employed people in the UK today.

As the leading member-led organisation representing small business owners and the self-employed, FSB is uniquely placed to contribute to this discussion. Since 1974 we have existed to represent those that run a business and to improve their circumstances. This report builds on this mission and the work we have undertaken since our inception to support those who 'go it alone'.

¹ Bank of England (BoE), 'Self-employment: what can we learn from recent developments?', 2015

² Julie Deane OBE, 'Self-Employment Review - an independent report', 2016

³ Baroness Michelle Mone OBE, 'Boosting enterprise in deprived communities', March 2016

SUMMARY OF FINDINGS

FSB surveyed 1,600 of our self-employed members last year. We sent the survey to members who 'go it alone' and therefore see themselves as self-employed in the general sense of the term. This included sole traders, freelance contractors, partners in small partnerships, as well as sole director limited companies (where the director is categorised as an 'employee' for tax purposes but in reality shares many of the characteristics of the self-employed).

The survey focused on the 'personal' side of self-employment, as opposed to the purely business considerations. It found, in keeping with other studies, that the self-employed are a highly diverse group, those working for themselves on a part time basis to those running multiple businesses. It includes young entrepreneurs and older business owners working for themselves as a means of boosting their income and staying active through retirement.

Among the key findings include:

- **Benefits of self-employment:** 39 per cent of self-employed people say the biggest benefit to being self-employed is independence at work, with 79 per cent say this is one of the top three benefits.
- 24 per cent of self-employed people say that 'being better able to balance work and personal/family life' is the biggest benefit of being self-employed with 61 per cent ranking this as one of the top three benefits. Women entrepreneurs (28%) were more likely than men (22%) to say this is the biggest benefit of self-employment. However, not all respondents feel the same, with some arguing instead that maintaining a good work-life balance is a significant challenge.
- 18 per cent of the self-employed say the opportunity to fulfil a personal vision is the biggest benefit, with 51 per cent ranking this in their top three benefits. Similarly, seven per cent say that 'having the opportunity to achieve something and get recognition for it' is the biggest benefit, with 38 per cent saying this is one of the top three benefits.
- **Challenges of self-employment:** most respondents suggest the biggest challenge facing the self-employed is not having certainty or security of income. 18 per cent say that 'not knowing how much income I will have from month to month' was the biggest challenge, with 44 per cent ranking this as one of the top three challenges. Similarly, 17 per cent of respondents say 'not getting paid if I fall ill or have to take time out of work for personal/family reasons' is the number one challenge, (44% listed ranking this as one of the top three challenges).
- 18 per cent of respondents say that finding and securing new business is the biggest challenge facing them, while 41 per cent place this as one of their top three challenges. Six per cent believe that 'being reliant on a small number of clients' is the biggest challenge, with 23 per cent denote it as one of the top three challenges associated with self-employment.
- **Income levels:** earnings among the self-employed vary significantly. 32 per cent of our survey respondents say they usually earn more than £2,000 a month⁴. By contrast, 41 per cent said they earn less than £1,000 a month, while 19 per cent earn less than £500 per month.
- Nearly two thirds (60%) of respondents say that since becoming self-employed they have experienced extended periods, lasting two weeks or more, when they have not been earning.
- 31 per cent of self-employed people have relied on the financial support of a partner/spouse due to not earning from self-employment, while 20 per cent have turned to a wider group of family and friends for financial support.
- **Savings and pensions:** Less than a third (31%) of our survey respondents said they were saving into a private pension. 27 per cent are planning to rely on their business to fund their retirement, while 20 per cent have other savings and investments which they intend to put towards their retirement. 16 per cent have property investments, such as buy-to-let properties. However, 15 per cent of respondents would appear not to have any savings to fund their retirement.

⁴ Estimated gross income

- **Access to other financial products:** one in five (21%) of our survey respondents said they had experienced difficulties accessing a mortgage because they were self-employed. This number rises to 40 per cent when considering only those respondents that had attempted to apply for a mortgage. In total, 14 per cent of respondents have experienced problems trying to get a business loan, while 13 per cent have experienced problems applying for a personal loan.
- **Personal insurance coverage among the self-employed is limited:** Under one in ten (9%) have income protection insurance to support them during periods of illness or when they are struggling for income.
- **Training and business support:** only 19 per cent of self-employed people have received training to assist them in their business in the past five years. Seven per cent had used a mentor during the last five years. Only six per cent have taken advantage of a Government-backed scheme providing business advice or support in the last five years.
- **Prior to becoming self-employed:** the majority of respondents were employed by another organisation (71%). 14 per cent were unemployed due to redundancy or leaving employment, while a further four per cent were unemployed but not looking for work (due to illness or caring responsibilities).
- **Ambitions for the future:** the majority of respondents (60%) plan to still be self-employed and running the same business in five years time. Slightly more women (64%) plan to still be running the same business than men (58%). Only four per cent of respondents expect to be in full or part time salaried employment in five years time.

Recommendations

Based on the findings from our research, this report puts forward a series of recommendations for Government to support the self-employed and address the challenges they face. Our recommendations are premised on the fact that when it comes to the self-employed, the boundaries between 'the business' and 'the personal' are very often blurred. They include the following:

- **Open up flexible saving and income protection insurance to the self-employed.** Government should work with industry to support the creation of more flexible saving products, which the self-employed can access, without penalty, when faced with a rainy day. It should also work with the insurance industry to develop more affordable income protection insurance options for the self-employed. This should include a specific focus on collective insurance models as previously recommended by FSB, IPPR and RSA, and cooperative models of savings, drawing on the example of Dutch 'bread funds'.
- **Assist and incentivise pensions saving among the self-employed.** The new Lifetime ISA offers welcome savings incentives for the self-employed, but is only accessible to the under 40s, while the self-employed are not currently being provided for by pensions auto-enrolment. With people working for longer, and many turning to self-employment later in life, other policy measures are needed to encourage saving. Government should prompt the self-employed to start saving - or increase their contributions - into a private pension or Lifetime ISA at certain stages, for instance, upon completion of their annual Self-Assessment. It should work with the pensions industry to explore the potential for greater flexibility in private pension savings and task the National Employment Savings Trust (NEST) with developing a bespoke default pension solution for self-employed savers. We also support the creation of a pensions dashboard, as recommended by the Financial Advice Market Review, to improve visibility of savings and help the self-employed make informed savings choices that suit their circumstances.
- **Address the discrepancies between the self-employed and employees in the social security system.** Building on recent changes to the single State Pension and childcare support, Government should do more to level the playing field for the self-employed. This includes bringing the Maternity Allowance closer in line with Statutory Maternity Pay, as recommended by the Deane Review, and exploring the feasibility of providing Statutory Paternity Leave and pay to all eligible self-employed fathers. Eligibility criteria for both benefits should continue to be based on National Insurance contributions, in order to maintain the contributory principle.

- Reform the tax system to support the self-employed and micro entrepreneurs.** FSB supports steps to enable the self-employed to conduct their tax affairs online but this must go hand in hand with wide-ranging simplification of the tax system. The Government should address concerns over plans to introduce mandatory digital tax reporting and press ahead with further simplification measures, building on the work of the Office for Tax Simplification (OTS). Specifically, it should explore the feasibility of creating a simplified tax regime for small businesses as recently proposed by FSB and EY, and engrain and enhance measures to support self-employment and entrepreneurship within the tax system. This includes taking steps to increase the new £1,000 tax allowance on trading and property income, to provide further support for micro-entrepreneurs and the self-employed.
- Reduce complexities within Universal Credit and make it more responsive to the realities of self-employment.** The Government should take advantage of delays in the roll out of Universal Credit by making changes to the policy for self-employed recipients. It should extend the start-up period to give claimants greater flexibility during difficult periods. It should also simplify reporting requirements, ensure they are compatible with tax reporting requirements and wherever possible avoid duplication. UC needs to support all viable forms of self-employment, including individuals with fluctuating profits and seasonal businesses and there should be equitable treatment for self-employed and employee recipients. As recommended by the Mone Review, the Government should ensure adequate support is available to new and existing UC recipients to enable them to grow their profits and income.
- Improve access to mortgages and other financial products for the self-employed.** The Government and the Financial Conduct Authority (FCA) should work with industry leaders to address barriers that prevent many self-employed individuals from accessing certain financial products. It should explore the feasibility of more flexible mortgage repayment terms for the self-employed and the possibility of lenders taking into account a wider range of business assets (including stock and outstanding future revenue) where self-employed mortgage applicants are unable to demonstrate sufficient proof of regular income. To inform this work, the Government should commission a review into access to mortgages and other financial products among the self-employed, with a view to implementing policy changes to open up access to these products. It should also work with sector regulators to take steps to ensure the self-employed and micro-entrepreneurs have adequate consumer protections in business-to-business markets.
- Reduce employment status uncertainty.** Lack of certainty of status is a constant concern facing the self-employed, in particular freelancers and those contracting with clients. FSB believes that bogus self-employment – whereby a small minority of employers falsely employ people on a self-employed basis to avoid NICs and employment rights – undermines genuine self-employment and should be tackled. However, the current intermediaries (IR35) legislation is complex, applied retrospectively and has failed to take into account the evolution in ways of working. It is also at odds with the definition of employment status in Employment Law. In addition to improving existing tools and guidance for users to determine employment status, the Government should explore the feasibility of introducing a single definition of self-employment, set out in statute. A legal definition would help to end uncertainty for self-employed and contracting businesses alike, prevent bogus self-employment and should also reduce enforcement activity and the high volume of case law in this area, cutting costs for the taxpayer.
- Improve business support for the self-employed and tackle late payment.** As the business support landscape in England evolves, it is important that relevant services and schemes are available for the self-employed, not just SMEs and high-growth firms. Similarly, the devolved administrations also need to ensure the self-employed are reflected in their business support offer. Government should act on the Mone review and improve the support offered under the New Enterprise Allowance scheme to ensure it equips self-employed recipients with the necessary skills to grow their business. Alongside this, education providers and business schools should improve signposting to online business courses and support the creation of

'school for start-ups' programmes as recommended in a recent FSB report⁵. Recipients of start-up loans should also be presented with an option to undertake training modules in areas such as leadership and management, thereby equipping themselves with skills that will benefit their business. Lastly, the Government should take further steps to tackle poor payment practices by commercial clients towards their self-employed suppliers. This includes strengthening the remit of the Small Business Commissioner to require it to 'name and shame' offending companies that breach payment terms, as well as providing access to low-cost commercial dispute resolution services to enable the self-employed to challenge unfair payment practices

•**Support home-based entrepreneurs to grow their business.** With a growing number of self-employed people running their business from home, the Government should build on recent reforms to facilitate home-based enterprise. Above all, it should prioritise the roll out of high speed broadband to all premises, delivering on its promise of a Universal Service Obligation guaranteeing minimum speeds of 10Mbps by 2020. Providers should also be challenged to focus on upload as well as download speeds and to set more stretching targets for quality of service agreements, including fault repairs and installation times. Local authorities, particularly those in urban areas, should work with enterprise support networks and other organisations to ensure adequate provision of shared work spaces for entrepreneurs, including serviced offices, co-location options and other, low-cost temporary work spaces.

⁵ FSB, 'Leading the Way: boosting leadership and management in small firms', 2016

SELF-EMPLOYMENT IN THE UK: AN OVERVIEW

The rise, the fall and the rise again of self-employment

Self-employment is booming in the UK. Signs suggest that the number of people in self-employment might soon outnumber those working in the public sector⁶. With one in seven people in the labour force now classified as self-employed, there is a clear need to understand who these individuals are, what motivates them and what their growth in number means for the future both of the UK's labour market but also the wider economy.

At the time when FSB was established in the early 1970s, self-employment stood at seven per cent of the labour force. This had remained fairly static since the end of the Second World War. The 1980s saw a significant increase in the numbers of people becoming self-employed, reaching 13.4 per cent of the workforce by 1992. During the boom years of 1997-2007 self-employment flat-lined and then fell⁷. However, following the financial crash of 2008, there was once again an increase in self-employment at a time when permanent salaried employment opportunities contracted.

Today, there are 4.6 million people, representing 15 per cent of the workforce, now working for themselves. Between 2008 and 2014, the number of people classified as self-employed rose by 732,000, accounting for over half of all job creation⁸. Furthermore, this trend has persisted even as the economy emerged from recession, with self-employment accounting for around a third of the growth in employment since 2010.⁹ Despite slowing marginally towards the end of 2015¹⁰, the long-term trajectory continues to be one of steady growth in self-employment.

In recent years there has been a debate as to whether the current period of rising self-employment is due to cyclical factors or whether a permanent structural change in the labour market is underway¹¹. The history of self-employment described above does indicate a close relationship between the economic cycle and the self-employment rate, suggesting that when there are fewer opportunities for permanent employment during or immediately following a period of economic contraction, more people end up working in self-employment until the labour market recovers. However, given we have seen a strong recovery in the UK labour market since 2008 alongside a continued increase in self-employment, the consensus now seems to be that we are indeed witnessing a structural shift.

This assumption is further backed up by evidence on the recent cohort of self-employed and why they have chosen to work for themselves. Research published by the Bank of England has found that relatively few people who lost their jobs following the financial crash went on to become self-employed.¹² Similarly, a recent survey conducted by the Department for Business, Innovation and Skills (BIS) found that only 16 per cent of self-employed respondents believed that a contributing factor to their choice to become self-employed was not being able to get an employee role. In addition, only a fifth of those surveyed planned to cease to be self-employed in the next three years, suggesting that most of the self-employed are happy with their current employment situation¹³. A separate RSA/Populus survey showed that less than one in five people started their own business because they had no other employment options. The overwhelming majority chose to go it alone because they wanted to¹⁴.

How does the UK's growth in entrepreneurship compare to other countries? Generally speaking, the rate of entrepreneurial activity in the UK has been higher than France and Germany but below that of the US¹⁵. However, high rates of self-employment do not necessarily correlate to higher entrepreneurial activity¹⁶ or strong economic performance. A recent IPPR study identified that the

6 RSA, 'Boosting the living standards of the self-employed', 2015

7 See CIPD https://www.cipd.co.uk/binaries/the-rise-in-self-employment_2012.pdf

8 Office for National Statistics, 'Self-employed workers in the UK', 2014

9 BoE, 2016

10 In the three months to January 2016, see ONS <https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/datasets/summaryoflabourmarketstatistics>. In the most recent estimate (for December to February 2016) self-employment increased by 11,000. See ONS, UK Labour Market, April 2016.

11 See for instance Andrew Henley 'The Post Crisis Growth in the Self-Employed: Volunteers or Reluctant Recruits?' <http://ftp.iza.org/dp9232.pdf>

12 BoE, 2016.

13 BIS, 'Understanding self-employment', 2016

14 RSA, 'Salvation in a start-up?', 2014

15 GEM Consortium, 'Global Entrepreneurship Monitor UK 2014 Report', 2015.

16 The US for instance scores highly on entrepreneurial activity metrics, but as a share of the workforce, has relatively low levels of self-employment.

economies of southern and eastern Europe have among the greatest share of self-employed workers: in Greece as many as 30 per cent of the workforce are self-employed¹⁷. However, this is in large part due to lack of salaried employment opportunities in these countries.

Since the financial crash, self-employment has remained fairly static across much of Europe, although in Germany rates of self-employment have been falling, which fits the view that the self-employment rate is closely linked to cyclical factors. However, the UK and the Netherlands are exceptions to this: both countries have witnessed a steady rise in self-employment, in conjunction with strong growth in employment, pointing to a permanent structural shift in both countries.

Who are the self-employed?

Who then is in this new army of the self-employed? When FSB was established in 1974, its founder, Norman Small, wrote the following in his founding statement:

'In my job as a representative calling on the retail trade and the self-employed - in the past five years I have talked individually to over 10,000 such people - the question of a non-party union for the self-employed has cropped up many times. And with fervour, I have been approached by such diverse people as a musician, a boat builder, an undertaker, a chimney sweep and a window cleaner, as well as hundreds of shopkeepers, to "do something" about it.'

(The Guardian, 31 August 1974)

The self-employed community was diverse then and has become ever more so today. Historically, the majority of self-employed people have worked in the construction and building trades and this remains the case. However, the recent growth in self-employment has been primarily in professional occupations including the education, technical information and communication sectors.¹⁸

Attempting to generalise the motivations and characteristics of such a diverse group is incredibly difficult to do. In order to make sense of this diversity, RSA has developed a useful framework which segments the self-employed into six groups, ranging from 'Visionaries', who are optimistic and growth-oriented business owners driven by a particular mission, all the way through to 'Dabblers', who are more often than not part-time workers who engage in business as a hobby and a means of doing something interesting in their spare time.¹⁹

One key demographic group that features heavily among the ranks of the self-employed is older people. According to the Bank of England, the ageing of the workforce accounts for around half of the increase in self-employment since 2004²⁰. Another key group is women: the number of women in self-employment has increased by 34 per cent since 2009, compared to 15 per cent for men.²¹ Indeed, a recent FSB report on women entrepreneurship suggests there remains significant untapped potential among women to start up and grow their own businesses²². Thirdly, there is evidence that many younger people are increasingly choosing self-employment over the relative security of a salaried job²³. Self-employment is becoming an increasingly attractive option for these three demographic groups.

As well as the demographic changes outlined above, technological advances have made self-employment an option for a greater number of people. The cost of setting up a business, for example computer equipment and advertising, has fallen over time relative to other goods and services. Advances in digital technologies mean that businesses can access a global marketplace from their own homes²⁴. It is also the case that larger companies increasingly value the flexibility offered by a specific subset of the self-employed, namely freelancers. These individuals are accessed by companies to provide specific expertise or to undertake individual projects, where in-house knowledge or skills are lacking. They can also drive performance and efficiency in that they provide important services to a

¹⁷ Hatfield I, 'Self-employment in Europe', January 2015

¹⁸ ONS, Labour Force Survey, 2014

¹⁹ RSA, 2014

²⁰ BoE, 2016

²¹ ONS, op cit

²² FSB, 'Women in Enterprise: The Untapped Potential', April 2016

²³ RSA 2014

²⁴ See Karabarbounis and Neiman, 'The global decline of the labour share', 2014.

business where an employee role is not appropriate.²⁵ Taken together, these developments would appear to indicate that the growth in self-employment looks set to continue in the years ahead.

The highs, the lows and the challenges for policymakers

As highlighted in the previous section, for the vast majority being self-employed is seen as a positive choice. According to BIS survey data, 84 per cent of self-employed people thought their life overall was better in self-employment compared with being an employee. The factors behind this appear to be greater flexibility, independence and job satisfaction.²⁶

Nevertheless, there are a number of challenges faced by many self-employed individuals, which are linked to their employment status. The BIS survey found that while half of those who are self-employed believe they are better off financially, around a third believe they are worse off. Reinforcing this, official data from the Family Resources Survey shows that the median earnings of people who work for themselves full-time are approximately 25 percent lower than their counterparts in waged work.²⁷ Similarly, a recent study by the Social Market Foundation found that nearly half of the UK's self-employed are in low pay²⁸, compared with around a fifth of employees²⁹. Despite earning less, the self-employed appear to be working more than employees, with twice the number of self-employed than employees working over 50 hours a week.³⁰ Inevitably these circumstances can lead to financial problems for some. Indeed, the evidence suggests that for an important minority, a lack of income when ill, a lack of long term savings and difficulties getting and paying for a mortgage are significant problems associated with their self-employment.³¹

Policymakers have been slow to respond to these challenges and only recently have issues such as average income levels among the self-employed come to the fore. Nevertheless, public policy has over the years affected and influenced self-employment in a number of ways.

Chief among these is the relationship between self-employment and the tax system. It is clear that tax policy can have a significant impact on an individual's decision to go it alone or otherwise. In 1995, the Inland Revenue changed the taxation rules in the construction industry, which undoubtedly contributed to the decision made by 200,000 self-employed workers to reclassify themselves as employees by 1997. Similarly, in April 2002, the Government introduced a change in the Corporation Tax rules which allowed directors of small firms to save income tax by taking their salaries as profits, thereby creating a tax incentive to become self-employed³². This change was accompanied by a corresponding rise in the self-employment rate.

A related issue is the lack of a legal definition of self-employment and the resulting uncertainty over the employment status of self-employed individuals. The TUC and Citizens Advice have raised concerns over this amid evidence of 'bogus self-employment', whereby employers employ workers on a self-employed basis in order to avoid National Insurance Contributions and employment rights.³³ Indeed, Citizens Advice estimates that around 1 in 10 of its self-employed clients should actually be classified as employees, which would amount to some 460,000 individuals. This not only impacts individual workers who do not receive many of the same protections afforded to employees (e.g. a legal right to receive the National Minimum Wage and access to Holiday Pay), but also on responsible businesses who want to do the right thing but are commercially undercut by rivals and ultimately the Exchequer which receives less in tax contributions.

Business groups including FSB have also long highlighted the problems caused by the lack of clarity over employment status, not least in the way in which HMRC applies and enforces intermediaries (IR35) legislation. Individuals who are operating on a self-employed basis – either as an individual sub-contractor or through a Personal Service Company – but deemed by HMRC to be 'inside IR35' (i.e. employees) are subject to significant penalties. Some 16 years after it was first introduced IR35

²⁵ See Andrew Burke, 'The role of freelancers in the 21st Century British economy'

²⁶ BIS, 2016; RSA, 2014

²⁷ See RSA, 2015

²⁸ As measured on an hourly, as opposed to monthly, basis.

²⁹ Social Market Foundation, 'Tough gig: Low paid self-employment in London and the UK', 2016.

³⁰ RSA, 2014

³¹ BIS, 2016

³² BoE, 2016

³³ For instance TUC, 2014; Citizens Advice, 2015. See also Standing, 2014

still commands strong opposition among freelance contractors, who believe the rules are applied arbitrarily and unfairly. Both the OTS and the recent Deane Review have recognised IR35 continues to be an issue, with the former recommending the merging of NICs and income tax³⁴ as a way of combating the problem while the latter has called for a single self-employment definition to be considered for tax and employment law.

Beyond the interlinked issues of tax and employment status, there has been relatively little attention paid by policymakers to addressing the living standards of the self-employed. Indeed, Ben Dellot at the RSA has pointed out that most government initiatives to support the self-employed are overwhelmingly centred on supporting businesses as entities in themselves rather than the individuals that sit behind these businesses. Similarly, efforts to tackle low pay have historically focused on increasing the minimum wage, yet this will not benefit self-employed workers. The Social Market Foundation (SMF) found that more than 1.7 million self-employed persons will earn less than the National Living Wage rate from 1st April 2016, which will increase to 1.9 million by 2020.³⁵

A key question is whether the UK's social security system is adequately geared up to this changing labour market and the growth in the number of people going it alone. On this, the Government has introduced several important changes in recent years. Reforms to the state pension system will now see the self-employed being able to access the full state pension for the first time, while similarly tax relief for childcare will be available to eligible self-employed individuals from 2017.

In other areas of welfare however, the self-employed face significant challenges. The introduction of Universal Credit (UC) is set to radically overhaul the welfare system and should better accommodate recipients with fluctuating incomes. However, in its current form, it will create a number of challenges for self-employed recipients. Currently, around 18 per cent of all self-employed people top up their earnings with Working Tax Credits or are in receipt of Child Tax Credit³⁶. Under the new system the self-employed will after a year see their UC award capped in line with a Minimum Income floor (MIF), which assumes they will be earning the equivalent of the minimum wage (or National Living Wage for the over 25s) over a standard full-time working week. In many cases, this could make them financially worse off. In addition, the accounting rules and reporting requirements under UC are onerous and fail to take account of standard business practices – a point that FSB have raised previously³⁷.

Furthermore, the financial support available to new parents who are self-employed has been identified as insufficient. The Deane Review called for the Maternity Allowance (MA), which is paid to eligible self-employed women for 39 weeks at a rate of either £139.58 a week or 90 per cent of their average weekly earnings if lower than the flat rate³⁸, to be brought into line with Statutory Maternity Pay (SMP). Unlike the MA, SMP pays employees a full 90 per cent of their earnings for the first 6 weeks, followed by the same entitlement as the MA for the remaining 33 weeks. Self-employed fathers, meanwhile, are not entitled to the equivalent of statutory paternity pay for employees, while self-employed adopters are not eligible for statutory adoption pay.

Saving for retirement is another important issue. Research shows that the self-employed are half as likely as employees to contribute to a pension³⁹, a difference that is set to be exacerbated as automatic enrolment is rolled out to all employees in the UK over the next two years. For many self-employed people on low or fluctuating incomes, it can be very difficult to put money aside towards a pension each month. Furthermore, unlike employees, the self-employed will not be 'nudged' into pension saving by being automatically enrolled into a scheme, nor will they receive an employer contribution towards a pension. As a result of differences in savings behaviour, it has been estimated the self-employed typically have a pension pot that is half the size of their employed counterparts at the point of retirement.⁴⁰ Government has recognised this problem, with the introduction of the new Lifetime ISA aimed among others at the self-employed.

34 OTS, 'The closer alignment of income tax and national insurance', March 2016.

35 SMF, 2016

36 Dellot B and Reed H, 'Boosting the living standards of the self-employed', 2015

37 See http://www.contractoruk.com/news/0010693rethink_self-employed_universal_credit_rules_ministers_told.html

38 There is also a 14 week maternity allowance worth £27 a week, available for self-employed persons who do not meet the eligibility criteria for the standard maternity allowance. This includes having to have worked for at least 26 weeks in the 66 weeks prior to the baby's due date, and earning at least £30 a week and paying class 2 NICs for at least 13 of these weeks.

39 See Resolution Foundation, 'Just the Job or a Working Compromise? The changing nature of self-employment', 2014.

40 RSA 2015

Obtaining and paying for a mortgage can also be a challenge for the self-employed, due in large part to fluctuating and uncertain income. Citizens Advice have found that average (median) mortgage debt for self-employed households is 8 per cent higher than for employee households, while between 2010 and 2012, 15 per cent of self-employed households with a mortgage reported that they struggled with their mortgage payments⁴¹. Accessing a mortgage in the first place can be problematic for self-employed persons, as lenders require proof of regular earnings for loan repayments – something which those on fluctuating earnings struggle with – alongside company accounts, SA302s or tax returns going back at least two years. While there are good reasons for this – not least to prevent unsecured lending of the type that occurred with the now banned self-certification mortgages – it can make it more difficult for the self-employed to get on the housing ladder.

In summary, being self-employed presents a number of unique challenges to a group of workers who often have very diverse needs. How the Government responds to this is a key area of focus for this report. The recent reviews, conducted by Michelle Mone and Julie Deane, show that a one size fits all approach is unlikely to address all of the current challenges facing the self-employed. Later on in this report, we set out several key areas where FSB believes the Government could best focus its efforts. In the next section, we explore in detail new survey evidence on the characteristics of the self-employed and the challenges they face.

⁴¹ Citizen's Advice, 'Going for Broke', 2016

FSB SURVEY FINDINGS

In order to improve understanding of self-employment, FSB decided to undertake a survey of self-employed persons within its membership last year⁴². The intention was to build on research and surveys carried out by others⁴³, rather than replicate what has been done previously.

We targeted FSB members who ‘go it alone’ and therefore see themselves as self-employed in the general sense of the term. We therefore included in this category members who were sole traders, freelancers, partners as well as one-person, single director limited companies, where the director is categorised as an ‘employee’ for tax purposes but shares many of the same characteristics of the self-employed. Some of our respondents had, subsequent to our last set of data, taken on employees. We have chosen to discount these respondents from the analysis below – focusing instead on those FSB members without staff.

Similar to other surveys, we asked members about the challenges and advantages of being self-employed, as well as a series of profiling questions. In asking these questions we were mindful of the fact that the average FSB member is more likely to occupy a certain type of category of self-employment – for instance, to be sole-traders or freelance contractors running their own businesses. Nevertheless, the survey still did unveil significant diversity in the ranks of the self-employed among FSB’s membership, which is in keeping with the wider profile of self-employment in the UK and therefore in our view is sufficiently representative.

The survey was completed by 2357 FSB members in total. 1600 surveys were completed by members that, at the time of being surveyed, did not have employees (the remainder had taken on staff since we had last profiled them). As mentioned above, the focus of our research is on those self-employed individuals that work ‘for themselves by themselves’ (i.e. they are without staff), and so for the purposes of our analysis, all data is based on the answers of these 1600 respondents, unless otherwise stated.

Profile of the self-employed I: gender, age, sector and professional status

We wanted firstly to explore the characteristics of FSB’s self-employed membership in detail – both to understand the extent to which our self-employed members reflect the diversity of the wider self-employed population, and to inform analysis presented later on in our research.

One third of respondents to our survey were women (33%), while the remaining two thirds (67 per cent) were men. This is in line with the national gender breakdown of self-employment in the official statistics⁴⁴. The average (mean) age of respondents was 56.69 years.⁴⁵ Women respondents (54.59 years old) were slightly younger on average than men (57.74 years old).

The sector profile of respondents was equally diverse. 12 per cent of respondents operated in business and real estate services, 10 per cent in wholesale and retail⁴⁶, eight per cent in information and communication, and a further eight per cent in arts, entertainment and recreation. In answering this question, respondents were presented with standard SIC code options. 29 per cent suggested ‘other’ – which would appear to reinforce the notion that many of the self-employed operate either across sectors or in niche or otherwise uncategorised sectors, such as the ‘sharing economy’.

When asked to describe their professional status, 45 per cent of respondents classified themselves as sole traders, followed by 27 per cent who said they were sole directors in a limited company. 16 per cent said they operated in a partnership, either as partners in an ordinary partnership (11%) or in a limited liability partnership (5%).⁴⁷ A relatively small number of respondents (four per cent) self-identified as being a freelance/contractor. This category was however more prominent in certain sectors, with marginally greater numbers of members operating in the IT sector (8%) self-identifying in this way.

42 The fieldwork dates for the survey were 3rd – 12th August 2015

43 Ipsos Mori poll for Resolution Foundation, 2014; Populus poll for RSA, 2014

44 See ONS, ‘Self-employed workers in the UK – 2014’

45 The median age of respondents was also 57 years.

46 The full SIC code is “Wholesale and retail trade; repair of motor vehicles and motorcycles”

47 Each of the latter three categories would usually be classed as self-employed for tax purposes, while sole directors of limited companies are treated as employees by HMRC (i.e they must pay Class 1 National Insurance contributions).

Profile of the self-employed II: duration, secondary employment, previous employment and reported income

The vast majority of respondents (77%) had been self-employed for more than five years. 27 per cent had over 20 years experience of self-employment. At the other end of the scale, 23 per cent had been self-employed for less than five years: eight per cent for less than two years, and four per cent for less than 12 months.

Women respondents were more likely than men to be new to self-employment, with 12 per cent being self-employed for less than two years compared to 6% of male respondents. Again, this statistic tallies with official data which suggests much of the recent rise in self-employment has been among women, many of whom are working self-employed on a part-time basis.

29 per cent of respondents had secondary employment, in addition to being self-employed. This includes working part-time as an employee for another company (6%), acting as a paid or unpaid non-executive director (4%) or doing other forms of voluntary work (13%). A further 13 per cent of respondents said they had more than one business. Nevertheless, for the majority (64%) of respondents their self-employment was their only form of work.

Prior to being self-employed, the majority of respondents were employed by another organisation (71%). 14 per cent were unemployed due to redundancy or leaving employment, while a further four per cent were unemployed but not looking for work – due to illness or caring responsibilities. A small number of respondents (3%) were students or in education before becoming self-employed, while for two per cent of respondents self-employment was a route back into work after a temporary period of retirement.

We also asked respondents about their income levels. Again, the responses suggested significant diversity for this group. Average (mean) income before tax and deductions totalled £1,858 per month. However, this figure masks significant differences in reported income. 8 per cent of respondents said they earned more than £5,000 a month, with a total of 32 per cent earned more than £2,000 a month. By contrast 41 per cent said they earned less than £1,000 a month, with 19 per cent saying they earned less than £500.

Perhaps unsurprisingly, the lowest earners were more likely to be working self-employed on a part time basis, with 57 per cent of those working less than 10 hours a week reporting self-employed earnings of less than £500 a month. At the same time, women were more likely to be earning less from their self-employment than men, with 51 per cent of self-employed women earning less than 1000 a month, compared to 36 per cent of men. Our data also found that self-employed women work marginally fewer hours than men (40 hours a week on average, compared to 43 hours for men).

Overall, our survey data reinforces previous research and official data⁴⁸ that many of the self-employed are on fairly modest incomes. However, income data for the self-employed should be treated with caution for a number of reasons. Firstly, survey data tends to capture a snapshot in time and therefore does not necessarily take into account fluctuations in self-employed earnings – a common feature of self-employment, which we will discuss in more detail later in this report. Secondly many datasets, particularly those based on household surveys such as the Family Resources Survey (FRS) tend to underestimate self-employed income and wealth.⁴⁹ We have no reason to believe that our survey is any different in this regard. A further challenge relates to differentiating income from investments and profits generated from the business, with many self-employed individuals choosing to reinvest profits back into the business rather than extract them in the form of an income. It is therefore important to take into account these caveats when examining income data for the self-employed.

⁴⁸ Resolution Foundation, 2014; Kirkby D, 'Standing alone? Self-employment for those on low incomes', Bright Blue, 2016; ONS, 2014b

⁴⁹ See for instance file:///C:/Users/1315/Downloads/ELMR_July07_Ormerod_tcm77-101217.pdf; https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/437481/family-resources-survey-2013-14.pdf and <https://www.iser.essex.ac.uk/research/publications/working-papers/iser/2015-15.pdf>

Benefits of being self-employed

We asked the survey panel what they felt were the biggest benefits to being self-employed. Respondents were asked to rank the options presented to them in order of importance, with one denoting the most important or biggest benefit and seven the least important, or smallest benefit. Respondents could also choose not to rank individual options, in order to show that they did not consider these options to be benefit at all.

According to the majority of respondents, the biggest benefit to being self-employed is 'independence at work'. 39 per cent of respondents selected this as their main benefit, with 79 per cent ranking this option as one of the top three benefits of being self-employed. Only 12 per cent of respondents chose not to rank this option, suggesting they did not consider it to be a benefit.

The second most popular benefit to being self-employed was the idea of being better able to balance work and personal/family life. This is often cited as a positive reason for working for oneself in surveys of self-employment, as the flexibility of being one's own boss, coupled with the lack of fixed working hours, enables individuals to manage work around other personal priorities. In total, 24 per cent of respondents selected this option as their number one benefit, with 61 per cent ranking it as one of their top three benefits. Respondents aged between 35-44 years and 45-54 years were most likely to cite this as the biggest benefit (34% and 30%) respectively, as were women respondents (28% compared to 22% for male respondents).

As shown in chart one, other benefits selected by respondents included having the 'opportunity to fulfil a personal vision' (with 18 percent selecting this as their number one benefit and 51 per cent ranking it in their top three) and 'having the opportunity to achieve something and get recognition for it' (7% and 38% respectively).

Interestingly financial benefits were seen as less important by respondents. Only six per cent selected 'earning more than if I were an employee in the same/similar line of work' as their number one benefit, while 20 per cent selected this as one of their top three benefits. This could be an indication either that they are earning lower incomes than they had hoped, or simply because income was not the main reason why they chose to be self-employed. Similarly, only one per cent said the primary benefit of self-employment was paying less tax (i.e. compared to if they were an employee for another company), with 10 per cent ranking this in their top three benefits.

Respondents were also given the option of stating other benefits to being self-employed. Among the answers given were the following:

"Ability to choose my working hours"

"Getting back to doing hands-on client work rather than just managing others"

"Choosing my own environment - both physical and in terms of the people I spend time with"

"Being able to change direction quickly if the market for my business' products changes"

"Not having to answer to anyone else and being responsible for my own future and business growth"

"Being able to work flexibly around the limitations of my disability"

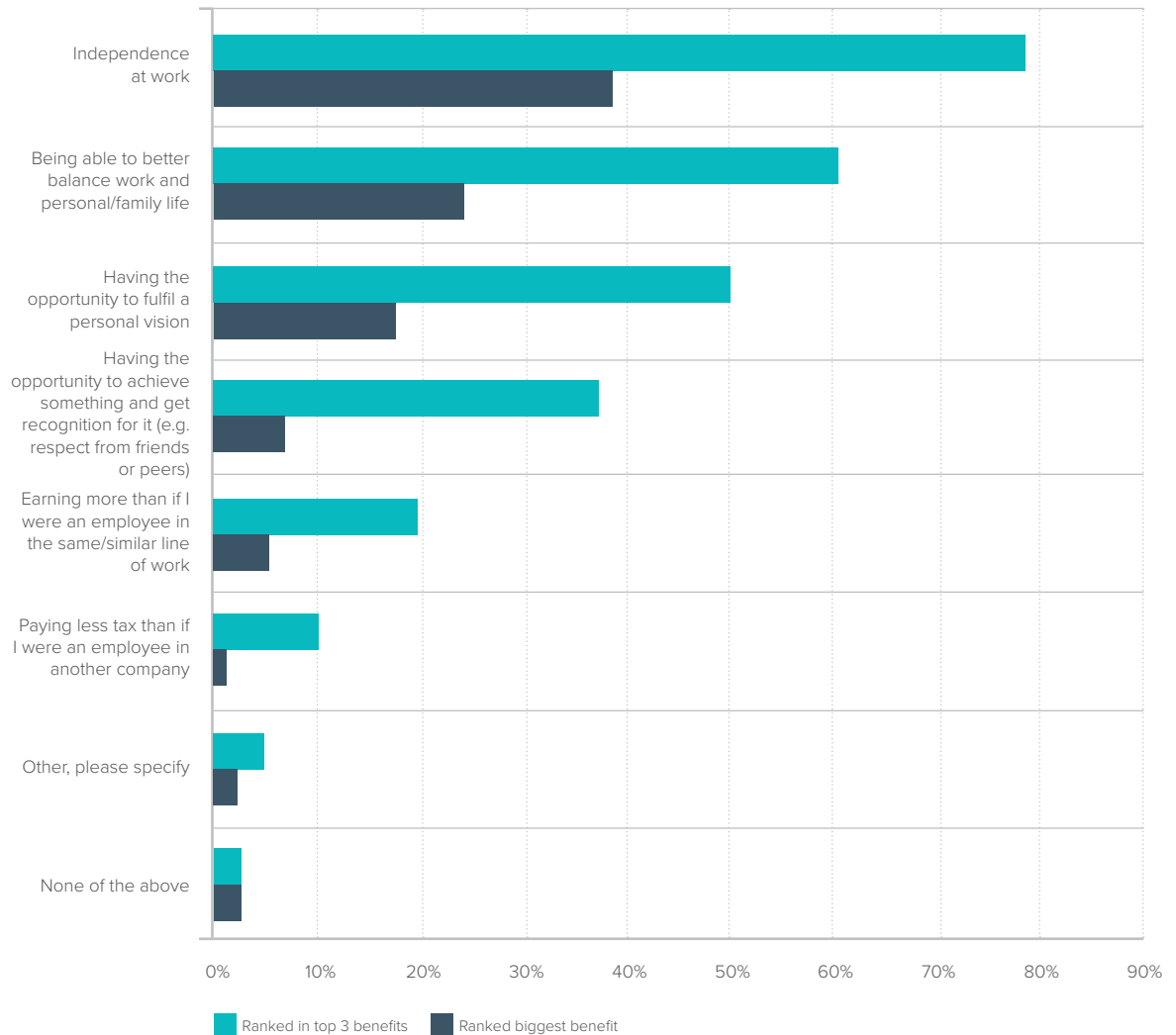
"Using skills and talents that I could not use in finding employment outside of creating my own business"

"Being active and intellectually stimulated"

"Creating a legacy and making a bigger contribution to British society"

The quotations listed above demonstrate the broad range of perceived advantages of being self-employed ranging from independence at work, a desire to perform a certain role or function, flexibility - both in terms of managing personal life but also business priorities - and also the desire to make an individual contribution to society or the economy.

Chart one: Benefits of self-employment, % of respondents by ranking (base: 1600)



Challenges of being self-employed

Respondents were also asked for their views on the biggest challenges of being self-employed. As with the question on benefits, they were asked to rank a series of options in order of importance.

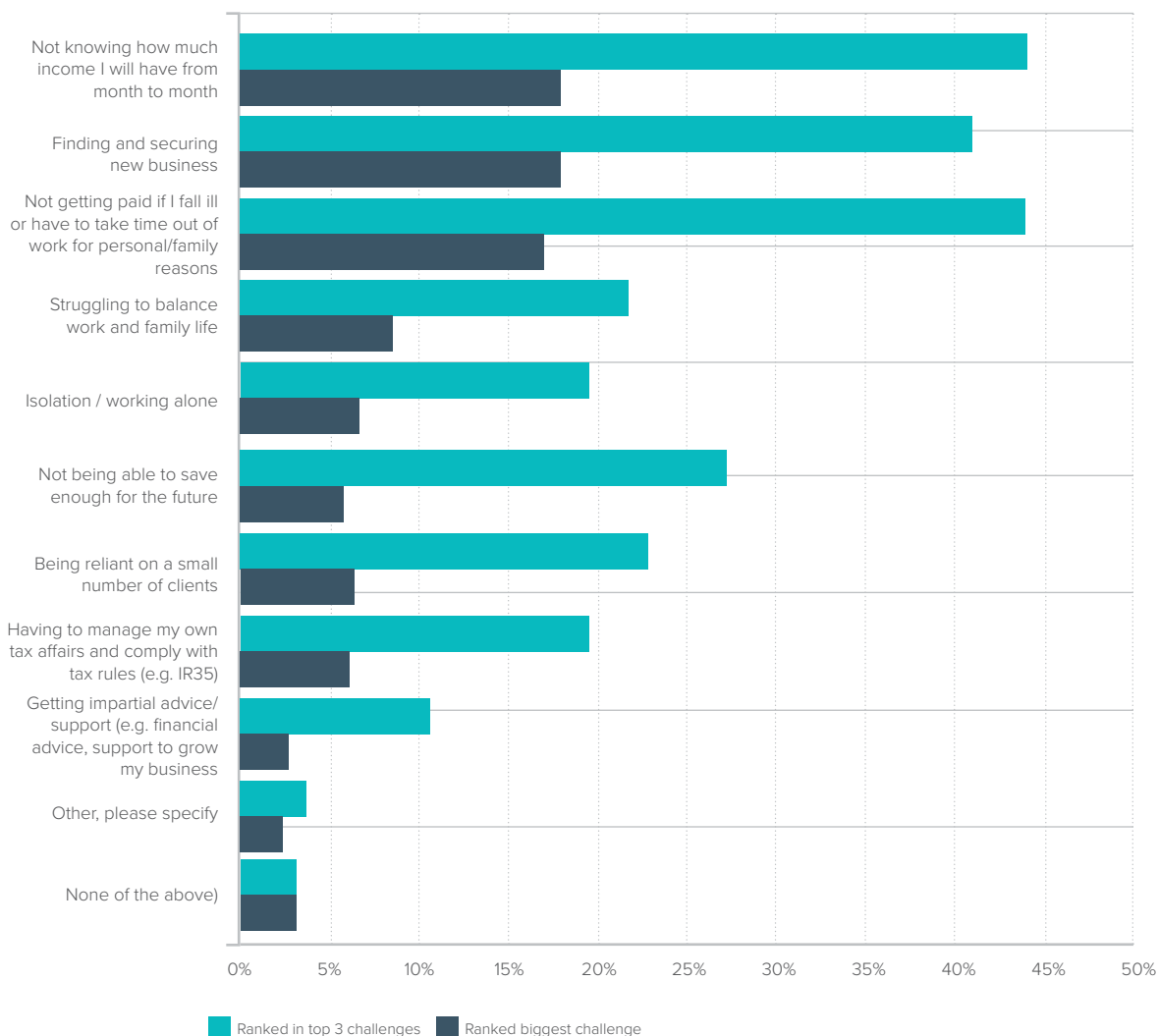
Our findings suggest that the biggest challenge facing the self-employed is a lack of both certainty and security of income (see chart two). 18 per cent of respondents said that ‘not knowing how much income I will have from month to month’ was the biggest challenge, with 44 per cent listing it as one of their top three challenges of self-employment.

Similarly, 17 per cent of respondents said ‘not getting paid if I fall ill or have to take time out of work for personal/family reasons’ was the number one challenge, with 44 per cent again listing this in their top three challenges. Only 26 per cent of members did not rank this option, suggesting it was not a problem for them. Women respondents and respondents aged between 45-54 years were more likely to say this was the main challenge of being self-employed.⁵⁰ The relatively high share of respondents selecting these options point to the difficulties caused by fluctuating earnings for the self-employed, which have wider financial implications such as for savings and accessing financial products – a point that will be explored in more detail below.

⁵⁰ 21 per cent of women said this was the biggest challenge compared to 15 per cent of men, while 20 per cent of those aged 45-54 said it was the biggest challenge, compared to 16 per cent for 16-34 year olds and 12 per cent for the over 65s.

A large number of respondents also suggested that ‘finding and securing new business’ was a challenge for them. This can often be the case for self-employed persons, particularly those starting up and looking for their first customers or contracts. 18 per cent of respondents said this was the biggest challenge facing them, while 41 per cent ranked this option in their top three challenges. Only 31 per cent of respondents suggested this was not a challenge. Similarly, not being able to grow their client base was also a concern for respondents, with 23 per cent ranking ‘being reliant on a small number of clients’ in their top three challenges associated with self-employment.

Chart two: Challenges of self-employment, % of respondents by ranking (base: 1600)



In contrast to the findings in the previous section, not all respondents agreed that self-employment was conducive to good work-life balance. On the contrary, many find maintaining a positive work-life balance a significant challenge. Nine per cent of respondents said that ‘struggling to balance work and family life’ was the main challenge of being self-employed, while 22 per cent listed this in their top three challenges. Having greater flexibility in work can be a particular challenge for the self-employed, as it can often equate to long working hours and not being able to switch off (i.e. due to a sense of obligation to clients, dealing with customer queries out of hours etc). Indeed, long working hours was something that many respondents suggested affected them, with 54 per cent suggesting that they regularly work more than 35 hours each week, half of whom (over 25%) regularly work more than 50 hours a week. Similarly finding the time to take a holiday can also be a challenge for many running their own business. Our survey found that respondents took 2.9 weeks of holiday on average

each year (mean) and while time off varies significantly across this group, 19 per cent said they take less than a week⁵¹ off each year, with five per cent saying they take no holiday at all.

Interestingly, relatively few respondents felt that putting money aside for savings was the biggest challenge of self-employment, with only six per cent stating that ‘not being able to save enough for the future’ was the biggest challenge - although 27 per cent listed this in their top three challenges. This may be because they feel they have sufficient savings as a self-employed individual, or because savings is not currently a priority for them – a point that we will return to in later sections.

Other, less prominent challenges included: isolation as a result of working alone, which again shows that independence at work is not universally regarded as a benefit by the self-employed (7% selected this as the main challenge, with 20 per cent selecting this in their top three challenges); ‘keeping skills and/or knowledge of my sector up to date’ (6% and 21% respectively) and ‘getting impartial advice/support – e.g. financial advice, support to grow my business etc’ (three per cent and 11% respectively).

Somewhat surprisingly, the number of respondents stating that managing their tax affairs and complying with tax rules was the biggest challenge to their business was relatively low. 6 per cent selected this as the main challenge, although 19 per cent selected this as one of their top three challenges. This may be due to several reasons, for instance use of accountants to manage their tax affairs. It is also worth noting that not all respondents may have been fully aware of measures announced at the 2015 Summer Budget, which took place a month before our survey was in the field. It is likely that many of these measures will pose significant challenges for the self-employed, such as changes to the way dividends are taxed (which will affect many single directors in limited companies) and plans to introduce compulsory digital tax reporting by 2020, which will require the self-employed to keep digital records and submit this data to HMRC online on a quarterly basis. This latter measure will pose significant challenges, in particular for those self-employed individuals who do not have access to the internet or currently use digital software for the purposes of running their business.⁵²

Other challenges quoted by respondents, which illustrate several of the above points, included:

“Too much work or not enough work”

“The time it takes to get paid by clients – it’s always longer than 60 days and sometimes more than 90 days”

“Not knowing how much work I’ll need to do from month to month”

“Not having pension contributions from anyone but me”

“Not ever really being able to step away from work even when on holiday or over the weekend”

“Not able to get a loan as the bank needs to see a regular income each month, even though the money will be available to support it.”

“Differential treatment by banks, notably around eligibility for mortgages”

“Earning less than if I was employed and with no employee benefits i.e. holiday pay. The government seems to think that everyone is employed and has employment protection but we do not”

“Attitude of HMRC toward small businesses and the self-employed”

“Having to do all the work, all aspects of the business... it’s really hard to find time to keep adding new work to my portfolio as well as doing all the admin/finance, keeping up to date with the industry and finding ways to try to attract new customers. I badly need an assistant but am not making enough money to afford one. Catch 22!”

⁵¹ Seven days

⁵² While HMRC have indicated there will be exceptions from mandatory digital reporting for the digitally excluded, and assistance will be provided for the ‘digitally assisted’, it remains to be seen how broad these categorisations will be.

Financial challenges

In addition to exploring the general perceived challenges of self-employment, we wanted to interrogate further the financial challenges experienced by the self-employed. As mentioned above, levels of reported income varied significantly across our survey respondents and depended on various factors, including the type of work they undertake. Furthermore, lack of fixed income is more likely to be a problem for some groups rather than others, for instance individuals working self-employed on a part time basis who are unable to rely on the income of a spouse or partner.

Nevertheless, the self-employed tend to be more prone than employees to experience certain financial challenges as a result of their employment status. As mentioned above, a key challenge identified by the self-employed is income volatility. Due to their lack of security of income, the self-employed can experience significant fluctuations in earnings and periods where they are not generating an income at all. Nearly two thirds (60%) of respondents said that they had experienced extended periods lasting two weeks or more since becoming self-employed when they had not been earning, compared to 37.5 per cent who had not.

The primary reason cited for an extended gap in earnings was a lack of business. 36 per cent of respondents stated that lack of clients or customers has meant they had endured periods without earning anything. This was followed by illness and health problems (22%), caring responsibilities e.g. for unwell relatives (9%) and starting a family/childcare (4%, rising to 10% for those aged 44 and under and nine per cent for women respondents). A further four per cent of respondents had experienced periods without earning an income due to being between businesses.

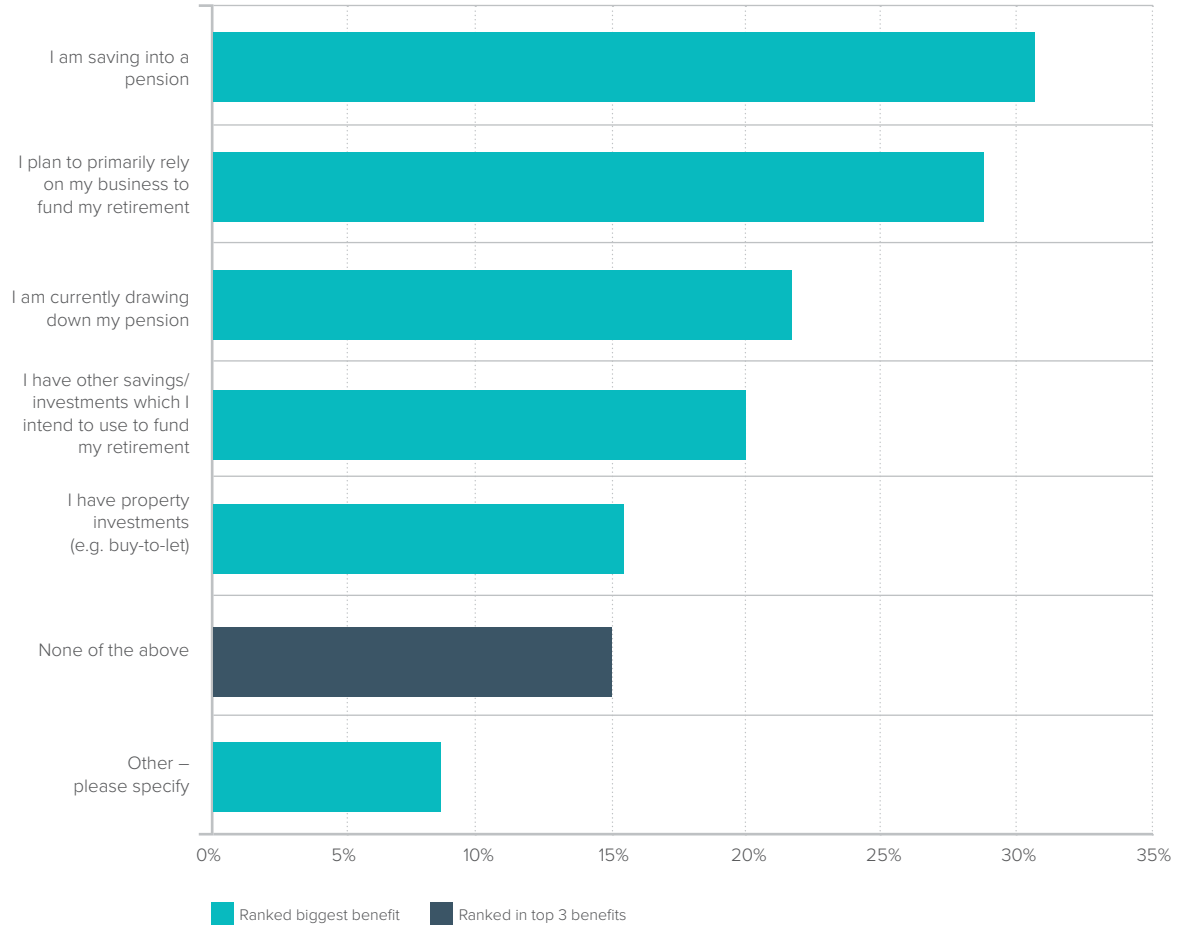
The problem of fluctuating earnings can also in part be linked to fluctuating hours of work. 14 per cent of respondents said the hours they worked varied significantly from one week to the next, while 67 per cent of respondents that worked varied hours also reported experiencing periods where they were not earning. However, working long hours does not necessarily equate to stable earnings either – on the contrary, 59 per cent of respondents working 70 or more hours a week experienced periods without earning anything, compared to 56 per cent working a regular 35 hour week.

Our survey found that a significant number of self-employed respondents have had to turn to family and friends for financial support in the past, due to not earning enough from their self-employment. 31 per cent of respondents have relied on the financial support of a partner/spouse due to not earning enough from their business, while 20 per cent have turned to a wider group of family and friends. A fifth of respondents (20%) said they have felt they would have to find an employee job, instead of pursuing their own business, were it not for the fact that their partner/spouse was earning as much as they did.

It is not just fluctuating income and gaps in earnings that are challenges for the self-employed. As previous studies have identified⁵³, the self-employed are often under-represented when it comes to savings. According to our survey, 31 per cent of respondents were saving into a private pension at the time of being surveyed (see chart three). In contrast, it is estimated that 59 per cent of employees are saving into pension scheme.⁵⁴ 22 per cent of our respondents said they were currently drawing down a pension (predominantly those aged 65 and above (6%)).

53 Citizen's Advice, *Shy of Retiring*, March 2016

54 See for instance <http://www.thepensionsregulator.gov.uk/docs/automatic-enrolment-commentary-analysis-2015.pdf>

Chart three: Savings and pensions, % of respondents (base: 1485)

As mentioned above, setting aside money each month to go towards a pension can be a significant challenge for many self-employed people, particularly those on low or fluctuating earnings. It is therefore unsurprising that levels of pension saving among the self-employed are also markedly lower than among employees. Again this gap is expected to grow as pensions auto-enrolment is rolled out to all employees. Under auto-enrolment, employees will benefit from an employer contribution and combined contributions are set to rise from three to eight per cent by 2019.

Of those self-employed individuals that are saving into a pension, contributions vary widely. On average, respondents report saving £295 (mean) into their pension each month. 14 per cent said they were contributing more than £500 a month, while 20 per cent were contributing less than £50 a month. Women self-employed were contributing on average less than men (£253 versus £315 per month respectively).

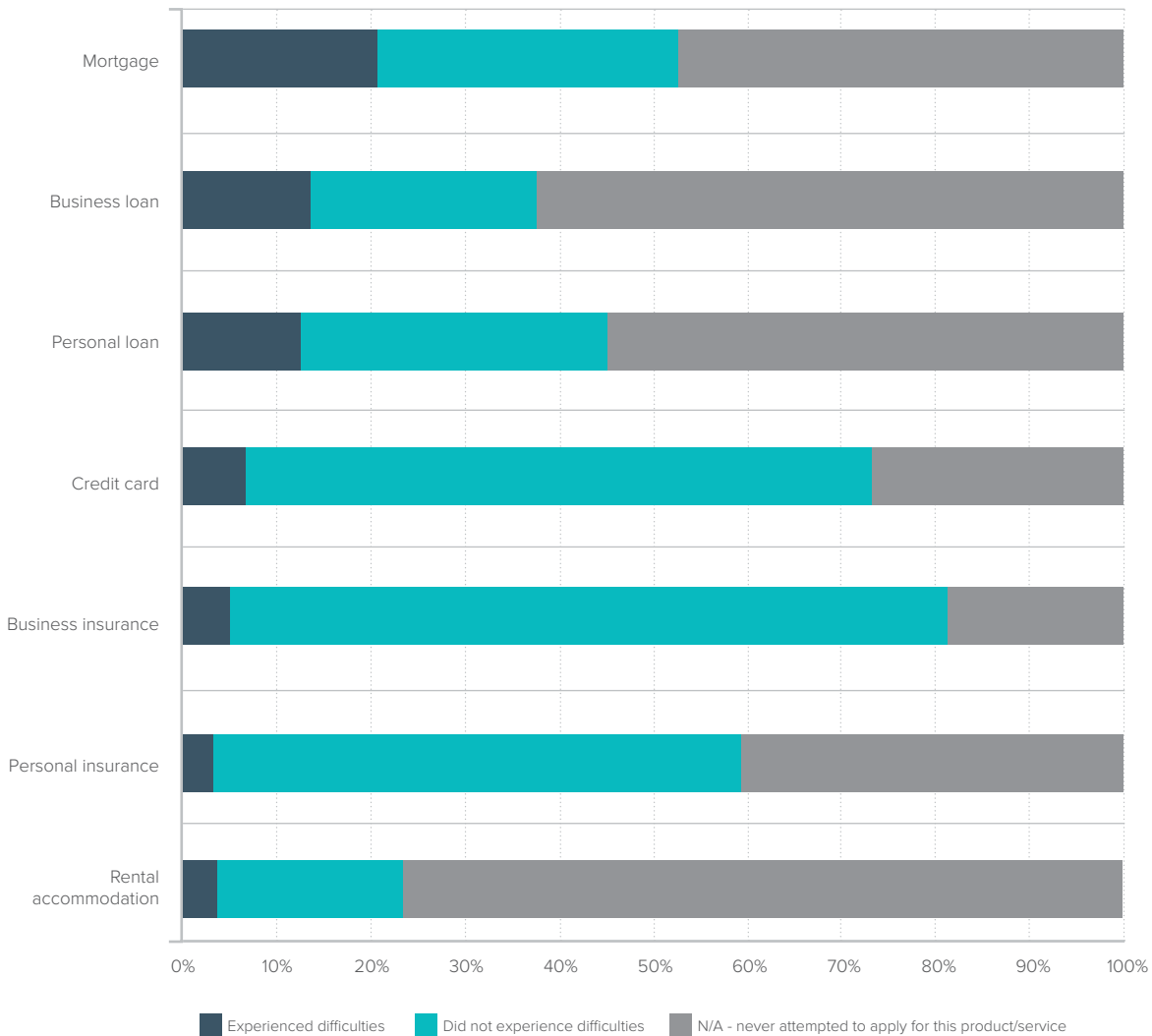
While the coverage and level of pensions savings appears to be limited, many self-employed persons are relying on other options to fund their retirement. 27 per cent of respondents said they were planning to rely on their business to fund their retirement, while 20 per cent said they had other savings and investments which they intended to rely on for their retirement. 16 per cent of respondents said they had property investments, such as buy-to-let – however, recent changes to buy-to-let rules, notably the three per cent surcharge on stamp duty, is likely to make this investment option less attractive in the future. While some self-employed individuals are taking advantage of multiple saving options to improve their chances of having a decent retirement income, this is not universally the case. In fact, 15 per cent of respondents selected ‘none of the above’ in response to this question, which indicates that they did not have a pension or any other long-term savings to fund their retirement (18% of women and 14% of male respondents selected this option respectively).

The self-employed can also struggle to access other financial products, such as mortgages, personal loans and insurance (see chart four). In total, one in five of our survey respondents (21 per cent) said they had experienced difficulties accessing a mortgage due to their self-employed status. When considering only those respondents that have applied for a mortgage (i.e. discounting those that have never applied for a mortgage), 40 per cent of respondents said they had experienced difficulties.

In total, 14 per cent of our respondents said they had experienced difficulties trying to get a business loan because they were self-employed (rising to 37 per cent when considering only those who have actually applied for a business loan), while 13 per cent struggled to get a personal loan (or 28 per cent when considering only those that had applied for a personal loan). Seven per cent of respondents in total said they had struggled to get a credit card (10% when considering only those who had applied for a credit card).

In total, four per cent of our survey respondents said they had struggled to rent accommodation because of their self-employed status. Of those that had applied for rental accommodation, 16 per cent said their self-employment status caused them difficulty.

Chart four: Experience of accessing financial products and services, % of respondents (base: 1600)



Relatively few respondents said they had experienced difficulties taking out either personal or business insurance (4% and 5% respectively). However, a relatively high number of respondents (40 per cent) said they had never attempted to access personal insurance: indeed, our findings indicate low levels of personal insurance coverage among the self-employed. Only 9 per cent of respondents said they had income protection insurance. While this is broadly in line with the working age average⁵⁵, the self-employed are more likely to be at risk given that they do not have access to statutory sick pay. Health insurance has a slightly higher coverage among the self-employed, but is still only taken out by a minority of respondents – 20 per cent had personal injury or accident insurance, compared to only 18 per cent with critical illness cover and 16 per cent with private medical insurance. A larger share of respondents (46%) had taken out life insurance.

While the above data highlight problems regarding the level of access and coverage of certain financial products for the self-employed, a related concern relates to consumer protections among this group. Previous research⁵⁶ has highlighted that business customers including the self-employed generally do not receive the same levels of consumer protection as individuals when interacting with other markets, such as financial services, energy and telecommunications. They are therefore disproportionately more at risk, should they receive poor advice or are miss-sold products.

This lack of protection is despite the fact that smaller business customers, and in particular sole traders and micro-entrepreneurs, are likely to face many of the same problems as individual consumers when buying products or services, especially when these are not directly related to their particular line of business. Micro-businesses find it difficult to navigate business-to-micro-business (B2Mb) markets due to limitations in their ability to access, understand and act on market information. They can also lack the purchasing power needed to access the best value offers. As a result, many markets are failing to deliver value-for-money products and services for many small businesses, including sole traders and micro-entrepreneurs.

Business, training and financial support

Respondents were asked about any business or financial support they had received during the last five years. 19 per cent had received training to assist them in their business (such as technical training or training on finance, management, administration and business strategy). Relatively few (7%) had used a mentor during this time.

Access to Government schemes among the self-employed also appears to be low. Only six per cent of respondents had taken advantage of a Government-backed scheme providing business advice or support, such as Growth Vouchers or the now discontinued Growth Accelerator scheme, while four per cent had accessed other business grants. The former may in part be due to the fact that many such schemes are targeted at high-growth firms and those looking to scale up, as opposed to the self-employed.

Furthermore, although 23 per cent of respondents had been running their business for less than five years, relatively few have accessed start-up support. Only two per cent of respondents in total had used a start-up loan, while one per cent had accessed the New Enterprise Allowance scheme, which provides financial assistance and mentoring support to unemployed individuals seeking to set up a business. That said, 15 per cent had received Working Tax Credit to top up their incomes. This figure was higher for women (18 per cent had accessed WTC over the past five years) than men (13%).

Although access to government-backed business support schemes does appear to be limited, this does not mean that the self-employed are not looking for advice or support or do not value the advice or support they have received previously. When asked what support they most valued⁵⁷ when the first became self-employed, half of respondents (50%) said tax advice, followed by advice on customer and supplier contracts (30%), advice on financing their business (28%) and training advice (21%). 15 per cent of respondents felt that the advice they received on business grants and financial assistance was the most valuable, while 12 per cent selected personal finance advice, including debt advice (see chart five).

⁵⁵ According to the ABI, 1.2 million people have individual income protection insurance, while a further 2 million have group-income protection insurance provided by an employer – which together equates to approximately 1 in 10 employees. See https://www.abi.org.uk/~/_media/Files/Documents/Publications/Public/2014/Protection/Welfare%20Reform%20for%20the%2021st%20Century.pdf

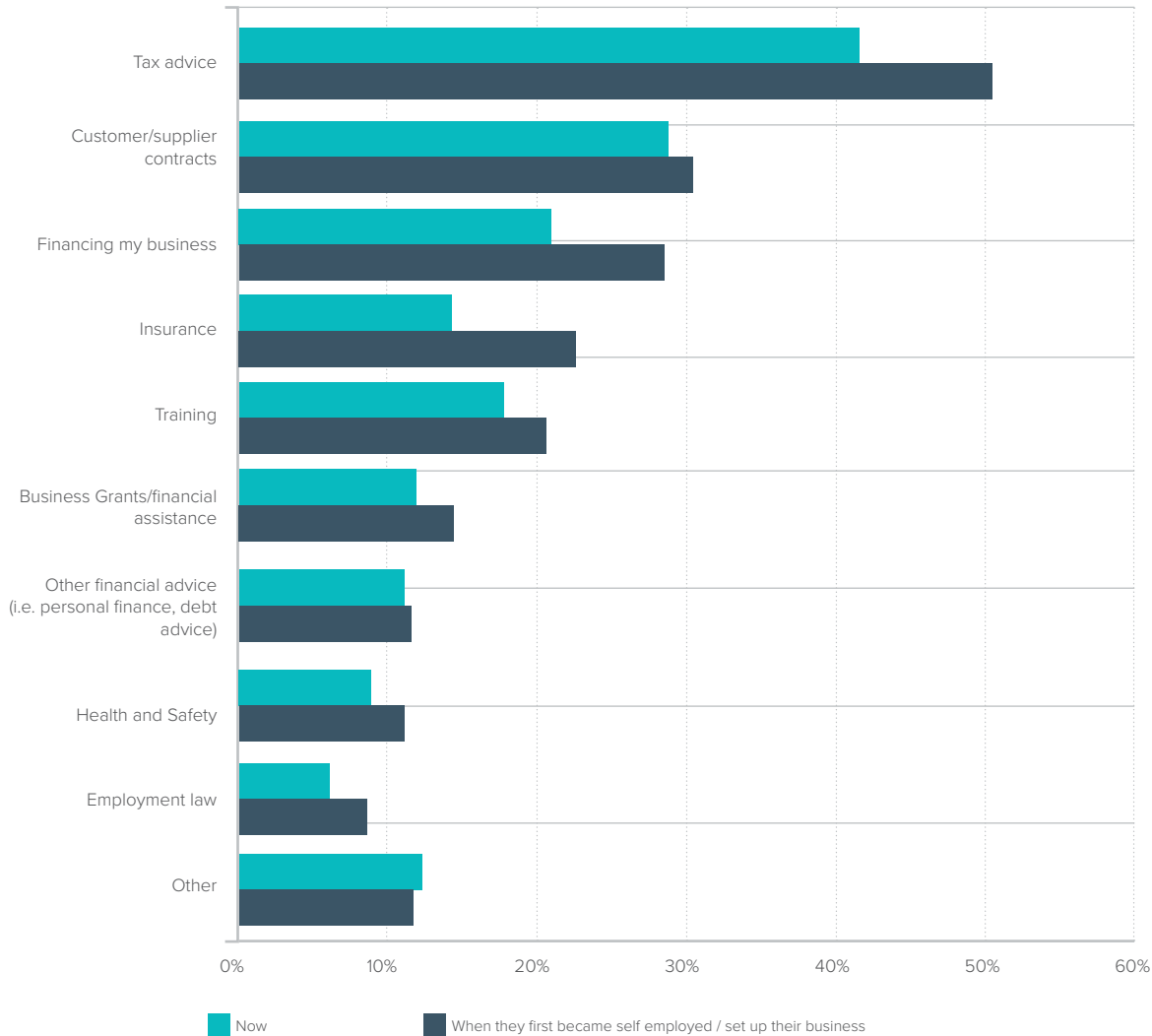
⁵⁶ Centre for Competition Studies and FSB, 'Small Businesses as Consumers: Are They Sufficiently Well Protected?', January 2014

⁵⁷ Respondents were able to select multiple options for this question

When thinking about the advice and support they value now, as opposed to when they first became self-employed, marginally fewer respondents (42%) selected tax advice although this was still the most popular response. The importance of tax advice is likely to reflect the complexity of the tax system for business owners, which is felt even among those who have been in business for some time.

Tax advice was followed by advice on customer and supplier contracts (29%), business financing (21%) and training (18%). 11 per cent of respondents suggested that other forms of financial advice, such as on personal finance and debt, were most valuable to them. The accessibility of advice in a number of these areas is likely to be impacted by several trends: for instance, the pace of bank branch closures⁵⁸ is likely to affect the ways in which sole traders source advice on financing their business in the future.

Chart five: Most valuable areas of business support/advice, % of respondents selecting each option (base 1600)



⁵⁸ The Campaign for Community Banking Services estimate that 681 closures took place in 2015.

Plans for the future

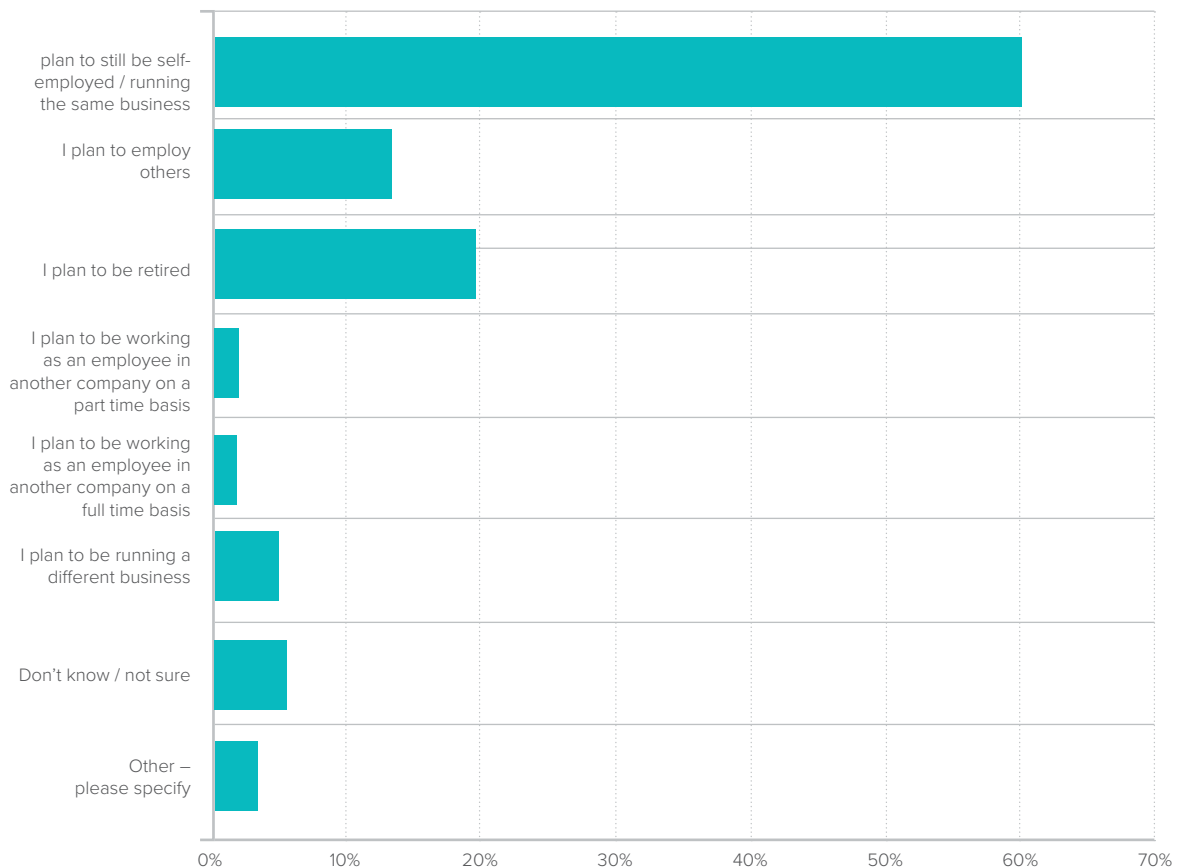
Finally, we asked survey respondents about their ambitions for their future and, specifically, where they see themselves in five years time (chart six). The majority of respondents (60%) said that they plan to still be self-employed and/or running the same business. This was more likely to be the case for women respondents (64%) than men (59%). A relatively small number of respondents expect to be running a different business (5%) in five years time.

One in five respondents (20%) said that they planned to be retired. For obvious reasons, this was more likely among older respondents. That said, among the oldest age category (the over 65s), only 48 per cent said they plan to be retired in five years time. This supports previous studies⁵⁹ which suggest that the self-employed are working for longer and plan to continue working later in life.

Interestingly, 13 per cent of respondents expect to be employing others in five years time. At the time of the survey, these individuals did not employ staff – and therefore in many cases they will be employing people for the first time. Equally however, the data suggests that many self-employed persons and sole traders have no intention of employing staff, preferring instead to continue to work on their own or grow their business in other ways (beyond hiring employees). This also points to concerns around legal obligations in the area of employment law.

A very small minority of respondents expect to enter into salaried employment. Only two per cent of respondents plan to be working as an employee in another company on a full-time basis in five years time, while two per cent expect to be a part-time employee for another company. This suggests that the vast majority of self-employed respondents expect to be working for themselves in the future and will choose to continue with their business.

Chart six: Where the self-employed see themselves in five years, % of respondents (base: 1600)



59 Citizens Advice and New Policy Institute, 'Who are the self-employed?', October 2015

RECOMMENDATIONS FOR POLICYMAKERS

The data presented in the previous section sheds further light on the profile of the self-employed in the UK today, alongside the benefits and drawbacks of going it alone. It also reinforces the findings of previous studies to show just how diverse the self-employed are as a group, not only with regards to the sectors and professions they span, but also their income levels, the degree to which they are affected by financial exclusion, and the types of business, training or financial support they seek. This is an important insight for Government policymakers, and suggests that while certain interventions may be appropriate for large numbers of self-employed people, few will be universally applicable – and that a more agile, targeted and smart approach to policymaking is needed if individual measures are to make a difference.

Nevertheless, there is a role for policymakers in helping to mitigate the challenges faced by many self-employed individuals, particularly those on low incomes. As mentioned earlier in this report, much of the existing policy in this space has focused on the challenges associated with growing a business, be that securing new customers, accessing finance or taking on employees. However, this report and others before it, including most recently the Deane and Mone reviews, have established that equally important are the personal challenges facing the self-employed.

The two sides of self-employment – the personal and the business - are of course closely interlinked, but it is this former category that is the primary focus of our recommendations.

1. Flexible savings and income protection insurance for the self-employed

As we have established in the course of this report, one of the biggest challenges facing the self-employed is not being able to rely on a secure income. This is rarely an issue for successful entrepreneurs with growing businesses, but for those new to self-employment and those struggling, it can be a significant problem – particularly in the absence of another income or family support to fall back on. Income volatility not only hits the self-employed when business is tough, but also when they or their family experience certain life events. The self-employed are financially worse off if they fall ill, as they are not entitled to sick pay, while they also run the risk of not earning in the event that they assume caring responsibilities.

Having less certainty over future earnings can also make the self-employed reluctant to put savings away – particularly in long-term savings and investment products that cannot be easily accessed. This has the further effect of diminishing the level of savings available to self-employed persons when they face a rainy day or when they reach the point of retirement.

In many ways, it could be argued that the above state of affairs is simply the reality of going it alone – and a necessary risk that the self-employed take. However, with self-employment now at an all time high and evidence of low-income self-employment increasing, FSB believe this is an area that needs addressing.

We therefore recommend that the Government work with industry to support the creation of flexible saving products designed with the self-employed in mind, which they can access when experiencing gaps in earnings or financial difficulties. These would operate on a similar basis to the recently announced Lifetime ISA (LISA), but could be used to cover a broader range of scenarios, for instance long-term sickness absence or caring responsibilities, rather than solely for the dual purposes envisaged for LISA⁶⁰. We note the Government's interest in exploring whether LISA savers could borrow against funds in their LISA, as is the case with 401k plans in the US⁶¹, for other purposes to provide additional flexibility. However, with the restrictions placed on the LISA and concerns over personal debt levels among the self-employed⁶², alternative savings vehicles should also be explored. These should offer competitive rates of return and enable flexible drawdown, without incurring significant tax penalties.

60 LISA funds will be available to use for pension saving or for a house purchase deposit for first-time buyers

61 <https://www.moneymarketing.co.uk/is-osbornes-lifetime-isa-the-shape-of-things-to-come/>

62 See Citizen's advice, 2016

In addition, Government should work with the insurance industry to open up affordable Income Protection (IP) insurance for the self-employed. According to our survey data, only nine per cent of self-employed individuals have IP insurance. Existing IP products can be expensive and more commonly purchased by large employers on a group purchase basis for their staff. In order to drive economies of scale, we recommend a specific focus on collective insurance schemes, similar to the model recommended by IPPR⁶³ to enable small businesses to provide occupational benefits such as enhanced maternity and sick pay to their staff – an idea that FSB has supported.

This model draws on the example of the DA-Barsel scheme in Denmark for employees⁶⁴, but would also be open to self-employed workers as is the case with a similar, government-backed insurance scheme in Quebec⁶⁵. Specifically, participants would pool regular contributions into a central fund, which could provide financial assistance in the event of parental leave or long-term sickness. Such a model could also be established and facilitated by sharing economy and other business platforms for their users⁶⁶. In addition, we recommend policymakers explore the potential for cooperative savings models to address their problem, drawing on the example of Dutch ‘bread funds’⁶⁷. These funds are local, small scale collective schemes, which are run and managed by small groups of self-employed persons themselves to prevent ‘adverse selection’, and provide income support for self-employed individuals facing financial hardship.

2. Assisting and incentivising pension saving

In addition to helping the self-employed weather difficult periods where they experience gaps in earnings, there is also a need to make sure they are sufficiently prepared for the long term and specifically, retirement. In recent years, policy-makers attention has focused on addressing the lack of pension saving among low-income and transient workers by introducing automatic enrolment. As a result, it is estimated that by the end of 2018, auto-enrolment will see over nine million employees saving into a workplace pension, many for the first time⁶⁸. However, as mentioned earlier, the self-employed are not being catered for by automatic enrolment.⁶⁹ As a result the gap between employee and self-employed pension saving is likely to grow, unless addressed.

As with the issue of income volatility, lack of pension savings is likely to affect certain groups of self-employed more than others – notably those with few or no savings or investments. The Government has in part recognised this with the introduction of the Lifetime ISA mentioned above, which offers a welcome incentive for the self-employed to save towards their pension. Savers will benefit from up to a 25 per cent contribution from the Government up to a total of £1000 a year and can draw down their savings tax free once they turn 60.

However, the LISA is only accessible to the under 40s and with people working for longer, and many people turning to self-employment later in life, it will not be an appropriate appropriate savings vehicle for all. Indeed, Citizens Advice and the New Policy Institute have found that 81 per cent or 740,000 of the increase in self-employed people since 2004/05 has come from those aged 45 or older⁷⁰. Furthermore, other more traditional savings options, such as buy-to-let property investments, have become less attractive to those self-employed who could otherwise afford second properties, due to increases in stamp duty.

FSB therefore believes that the Government should explore additional measures to encourage pension saving for the self-employed and work with the industry to develop appropriate solutions. This would be a holistic exercise, with a view to identifying both short-term and long-term savings solutions and recognising the desire for flexibility over saving among the self-employed. Specifically, the Government should task NEST, the government-backed auto-enrolment provider, with developing a bespoke, default flexible pensions saving solution for self-employed savers. As with existing workplace pension schemes, contributions would continue to benefit from tax relief in order to incentivise saving.

63 See Thompson S, ‘Small firms, Giant Leaps: small businesses and the path to full employment’, April 2014

64 http://www.atp.dk/X5/wps/wcm/connect/dab/com/index/about_da_barsel#.UOWPL6Keaf5

65 http://www.rqap.gouv.qc.ca/travailleur_autonome/types/maternite_en.asp

66 See <http://www.ft.com/cms/s/0/b1d854de-169f-11e5-b07f-00144feabd0.html>

67 See <http://www.theguardian.com/sustainable-business/2014/sep/15/payment-insurance-co-ops-netherlands-uk-bread-fund>

68 See <https://www.gov.uk/government/news/millions-more-saving-thanks-to-automatic-enrolment>

69 Although business owners, such as directors in limited companies, can technically opt in if they wish.

70 Citizens Advice and New Policy Institute, 2015

In addition to providing tailored schemes, a key challenge facing policymakers is to normalise pensions savings for the self-employed. Employees are benefitting from the ‘nudge’ of auto-enrolment⁷¹, however this is not currently possible for the self-employed given the absence of an employer to auto-enrol them into a scheme. As a result, Government should explore ways in which it can prompt the self-employed to start saving - or increase their contributions - into a private pension (or indeed a lifetime ISA) at certain recognisable stages, for instance, upon completion of their annual self-assessment to HMRC. Citizen’s Advice have explored this idea in some detail. They suggest that the introduction of digital tax accounts for the self-employed could include a tick box option, whereby selecting this would opt the self-employed in to a pensions scheme.⁷²

Normalising pensions saving among the self-employed also requires the industry to improve transparency of savings and pensions. We therefore support the creation of a pensions dashboard, as recommended by the Financial Advice Market Review⁷³. This should improve visibility of savings and help all savers, including the self-employed, to make informed savings choices that suit their circumstances.

3. Addressing the discrepancies between the self-employed and employees in the social security system.

The self-employed have historically received a lower level of social security entitlements than employees. This is partly a result of the design of the contributory welfare system and the fact that the self-employed tend to pay less National Insurance than employees. More broadly, it reflects yesterday’s labour market – namely, one with very low levels of self-employment. With the growth in self-employment at record levels and showing few signs of abating, it is time to reform the system of social security so it better reflects today’s economy.

The Government has in part accepted this argument and in recent years has made important changes to entitlements for the self-employed. As mentioned above, reforms to the state pension will see the self-employed able to access the full state pension for the first time, while from 2017 they will also be able to access tax relief on childcare, through the Government’s tax free childcare scheme.

FSB supports the recommendations of the Julie Deane Review which argues that the Government should go further in addressing the mismatch in entitlements and level the playing field for the self-employed. Specifically, we recommend it brings the Maternity Allowance closer into line with Statutory Maternity Pay. It should also explore the feasibility of providing Statutory Paternity Leave and Pay to all eligible self-employed fathers⁷⁴, as well as extending Adoption Pay and Shared Parental Leave Pay to the self-employed.

Access to entitlements should be based on set eligibility criteria, including the requirement to have made sufficient National Insurance contributions in a given period. As has been proposed by IPSE, payment of 90 per cent of average earnings for the first 6 weeks of maternity leave for a self-employed individual could be calculated based on average earnings over the previous 12-24 months to allow for fluctuating earnings⁷⁵. As part of its consultation exercise into reforms to self-employed NICs, the Government should examine how these entitlements could be built into the contributory framework in a way that is simple, fair and remains accessible to self-employed persons on low or fluctuating incomes⁷⁶.

⁷¹ Auto-enrolment draws on insights from behavioural sciences, which suggest individuals that have been opted in to a pension are more likely to remain in the scheme than make an active decision to opt out.

⁷² Citizen’s Advice, ‘Shy of Retiring: Addressing under-saving among self-employed people’, January 2016

⁷³ See <https://www.fca.org.uk/static/fca/documents/famr-final-report.pdf>

⁷⁴ The eligibility rules are currently confusing, i.e. directors of limited companies who pay themselves via PAYE and pay class 1 NICs can claim SPP

⁷⁵ See IPSE <https://www.ipse.co.uk/policy/maternity-pay-policy-briefing>

⁷⁶ This includes ensuring that voluntary Class 3 contributions, which the self-employed can pay to address gaps in the National Insurance record, are affordable. Proposals outlined in HM Treasury’s consultation would see a sharp uplift in the cost of Class 3 contributions (£14.10 a week), compared to current Class 2 rates (£2.80 a week) for essentially the same level of entitlement, which would negatively impact many self-employed individuals.

4. A tax system that supports the self-employed and micro entrepreneurs

Alongside the social security system, the tax system also needs to better reflect the growth in the number of people going it alone and the realities of self-employment. An optimally designed tax system would significantly reduce the burdens of tax administration on the user, foster and reward risk-taking and entrepreneurship, while at the same time generating sufficient receipts for the Exchequer. However, evidence suggests that small business owners find the tax system among the most complicated area of legislation⁷⁷ and often feel they face little option than to spend money on tax advice or run the risk of non-compliance. Furthermore, the complexity of the tax system can also make it difficult for many self-employed people to understand the link between national insurance contributions and benefit entitlement⁷⁸.

In addition, the Government has recently introduced a series of measures, primarily aimed to boost the tax take among the self-employed, which will create additional administrative challenges and costs. This includes changes to dividends taxation, altering IR35 rules for those sub-contracting with the public sector and, from 2020, requiring the self-employed to keep digital tax records and submit quarterly tax returns to HMRC online.

While efforts to enable the self-employed and small firms to conduct more of their tax affairs online appear advantageous, the benefits will only be realised if this goes hand in hand with structural simplification of the tax system, alongside further steps to help the self-employed. Measures outlined in the recent Business Tax roadmap⁷⁹ provide an important starting point for reform, with plans to introduce a dedicated HMRC phone line for small businesses particularly welcome. However, more needs to be done. This includes taking forward work planned by the OTS to examine new business models that seek to protect the assets of the self-employed – many of whom trade with unlimited liability, which mean that personal assets, including their home, are at risk. We also recommend the Government and the OTS explore the feasibility of moving towards a radically simplified tax regime for small businesses as recently proposed by FSB and EY⁸⁰, which would include the amalgamation of several taxes into a single proxy rate of tax owed.

Finally, policymakers should also engrain within the tax system measures that reward self-employment and micro-entrepreneurship, such as the recent extension of entrepreneurs relief and the new £1,000 tax allowances on property and trading income announced in the 2016 Budget. Under this latter measure, the self-employed will not need to pay or declare income tax on trading or property income below the allowance threshold. We recommend that Government considers increasing these allowances further, to £2,000, in order to provide further support and reduce tax administration for micro-entrepreneurs and the self-employed.

More generally, we need to see further changes in the way in which HMRC interacts with the self-employed, with far more focus given to supporting the self-employed grow their business, in line with HMRC's new duty to promote economic growth. Overall, the aim should be a simplified tax regime for the self-employed, which entails minimum administration and greater certainty for small business in knowing what their tax liability will be – enabling them to get on with running their business, plan investments and grow, including taking on staff.

5. Reducing the burdens of Universal Credit for the self-employed

Our survey found that currently 15 per cent of the self-employed access working tax credit to top up their incomes. This safety net provides valuable support to those on the lowest incomes and who experience fluctuations or gaps in earnings, such as seasonal business.

As mentioned previously, the Government is replacing WTC with Universal Credit. The rules for the self-employed are complex and impose additional conditionality requirements on self-employed recipients. In addition to reporting for tax purposes annually (and potentially in the future on a quarterly basis), the self-employed will be required to report their income and expenditure to DWP

⁷⁷ FSB, Barriers to Enterprise survey, October 2013

⁷⁸ Citizens Advice, Response to OTS Report on alignment of National Insurance with Income Tax, 2015

⁷⁹ HM Treasury, 'Business Tax Roadmap', March 2016

⁸⁰ FSB and EY, 'A new approach to simplifying taxation for smaller businesses', December 2015

each month on a separate accounting basis⁸¹. In addition, after an initial start up period, self-employed UC recipients will be subject to the Minimum Income Floor (MIF), which will cap their UC award in line with an assumed level of hourly earnings, which is set as minimum wage/NLW for a full-time working week. Those earning less than the minimum wage for hours worked in any individual month stand to lose out.

While steps have been taken to more closely align UC reporting rules with HMRC processes, we remain concerned about the impact of the rules on the self-employed. We therefore recommend that Government takes advantage of the fact that Universal Credit has yet to be rolled out in full to make several important changes to the rules.

Firstly, UC must be compatible with all viable self-employed businesses, including those with fluctuating profits and seasonal businesses, such as farming where due to the nature of the sector the vast majority of income is received in certain months during the year. As part of this, it should extend the start-up period – where the MIF will not be applied - to allow claimants greater flexibility during difficult periods beyond the first year of trading. It should further take steps to simplify reporting requirements and ensure they are compatible with changes to tax reporting requirements to avoid unnecessary duplication. The rules should also provide for far more equitable treatment for self-employed and employee recipients of Universal Credit, for instance with regards to the treatment of pension contributions under the MIF.

In addition, clear guidance and support needs to be made available to UC recipients so that they fully understand the rules and can improve their chances of growing their business. We welcome the Government's intention, announced in the 2016 Budget, to trial face to face business support and mentoring for UC claimants. As recommended in the Mone review, Job Centre Plus need to do far more to support and advise new UC recipients on ways to grow their business income, including by signposting them to appropriate business support schemes in their locality. However, alternative options should be explored for existing UC recipients, who will not necessarily come into contact with JCP staff, to enable them to boost their income – and ultimately move off Universal Credit.

6. Improving access to mortgages and other financial products

As discussed above, many self-employed persons can often struggle to access mortgages and other financial products. This can often be due to not being able to verify past income or demonstrate a regular future income, with lenders legitimately concerned over the ability of borrowers to afford repayments.

This problem has been raised specifically in regard to mortgages, which in many ways has been made more difficult by changes in legislation following by the Mortgage Market Review. This brought an end to self-certification mortgages, which required little or no proof of income and led to examples of risky and irresponsible lending to self-employed applicants. However, with evidence that the self-employed more than any other group struggle with mortgage access, this is a problem that needs addressing.

The Government and the Financial Conduct Authority (FCA) should work with industry leaders to address barriers that prevent many self-employed from accessing these financial products. It should explore the feasibility of providing more flexible mortgage repayment terms for the self-employed. This is similar to the idea of a 'right to request' flexible repayment terms as proposed by RSA, however the FCA would need to work closely with the industry to assess the risks involved and mitigate the impact this would have on repayment periods and interest incurred. To enable the self-employed to access mortgages, it should explore the feasibility of lenders taking into account a wider range of business assets (including stock, profits retained in the business and outstanding future revenue e.g. as a result of late payment of invoices), where self-employed mortgage applicants are unable to demonstrate sufficient stability of income. While some lenders give consideration to retained profits, business plans and new contracts that have been secured when assessing a mortgage claim, this is not universally the case.

⁸¹ For businesses that do their tax computation using HMRC's simplified basis, UC accounting will be similar in terms of the actual figures used. However, for self-employed businesses that account for their tax on an accruals basis, the differences with UC accounting are substantial.

Such a move would provide lenders with additional evidence about the financial suitability of self-employed borrowers, in addition to previous business accounts, tax records and credit scores which are currently used by mortgage lenders to determine suitability. It would also help the newly self-employed, who are growing their business, but do not have accounts or self-assessment returns for the previous 2-3 years to demonstrate past income, which is usually a requirement for many mortgage lenders⁸².

To inform this work, the Government should commission a review into access to mortgages and other financial products such as personal insurance among the self-employed and explore further ways of opening up these products. Separately, it should work with sector regulators to take steps to ensure the self-employed and micro-entrepreneurs have adequate consumer protections in financial services and other business-to-business markets, such as telecommunications and energy. This includes improving access to commercial redress for micro businesses, including use of alternative dispute resolution.

7. Reducing uncertainties over employment status for the self-employed

One of the biggest challenges facing the self-employed is determining and proving their self-employment status. Lack of certainty of their status is a constant concern facing the self-employed, in particular freelancers and those sub-contracting with clients, who must ensure that the work they carry out is outside of the scope of IR35 rules. At the 2016 Budget, the Government proposed to tighten these rules further by placing a new duty on public sector engagers of contractors operating as personal service companies to determine IR35 status. Where an individual is found to be within the scope of IR35, significant penalties can be applied.

Furthermore, and as mentioned above, Trade Unions and other groups have raised legitimate concerns about ‘bogus self-employment’ – a practice whereby employers place individuals who are effectively working as employees on self-employed contracts, in order to avoid NICs and employment rights. FSB believes that bogus self-employment undermines genuine self-employment and entrepreneurship and should be tackled. Nevertheless, it is also the case that the complexity of the current status regime causes significant problems for self-employed individuals and their engagers alike in determining status. The current IR35 rules give rise to different interpretations and, in being enforced retrospectively by HMRC, lead to individuals running the risk of being found to be in scope of IR35 and therefore incurring time-consuming enforcement investigations and penalties. Constantly evolving case law in this space also provides further complexity for self-employed individuals and businesses.

A key challenge is that employment status in tax legislation (where an individual is either an employee or self-employed) is inconsistent with employment status as prescribed in Employment Law. Unlike in tax law, employment law includes a third status, that of the ‘worker’. In line with the Deane Review, we recommend the Government explores the feasibility of more closely aligning the two interpretations of status⁸³, with a view to establishing a single definition of self-employment, set out in statute⁸⁴. This could inform the creation of a ‘statutory employment test’, an idea which has been explored by the Office for Tax Simplification,⁸⁵ which would sit alongside accompanying guidance that reflects the different categories of self-employment (e.g. sole trader, freelance contractor etc). Together, these measures would provide users with far greater upfront clarity as to their likely status. Within Government, this should also enable a more joined up policy on self-employment, aligning the approach of HMRC with that of BIS, DWP and other departments that traditionally seek to promote entrepreneurship.

A single definition is likely to create winners and losers, but would go a long way to addressing the problems caused by the current regime – which has failed to keep pace with the changing nature of employment and evolution in ways of working. Furthermore, it should enable the vast majority of freelancers who operate genuinely on a self-employed basis, to continue to provide valuable services,

⁸² A number of lenders are now considering self-employed applicants with one year of accounts.

⁸³ Regarding this recommendation, we note that full harmonisation is unlikely and it would be impractical to remove the ‘worker’ status from Employment law, given the importance of agency workers to the economy.

⁸⁴ The Deane Review makes a similar recommendation stating that ‘a single definition for tax and employment law is desirable and should be considered’.

⁸⁵ OTS, Employment Status report, 2015

skills and flexibility sought by corporations and small businesses alike. Above all, it should also help to end uncertainty for self-employed and contracting businesses, prevent bogus self-employment and in theory should reduce enforcement activity and the volume of case law too, cutting costs for the taxpayer.

We appreciate that the above reforms would take time to develop and are not straightforward. In the meantime, Government should press ahead with plans⁸⁶ to simplify the IR35 tests and develop a new and improved online tool to help individuals and businesses determine employment status more effectively. In the longer run, when the public finances allow, the Government should lower the rates of class 1 NICs for both employers and employees (i.e. primary and secondary contributions), bringing them closer in line with self-employed (class 4⁸⁷) NICs. This should reduce the incentive for employers to hire workers off payroll, thereby reducing the incidence of bogus self-employment. Lowering primary class 1 NICs would also be in keeping with the Government's stated aim of cutting taxes for the lowest paid, in line with its policy to raise the personal tax allowance.

8. Widening the business support offer to the self-employed and tackling late payment

Our research has found that self-employed individuals value the external support and advice they have received, both when they started up in business and once they became more established. However, relatively few have accessed government-backed business support schemes, while only 16 per cent have undertaken training to help them run their business.

The decision not to access government-backed support schemes is likely due to a number of reasons. This includes a lack of visibility of the schemes available, resulting in part from the complexity of the business support landscape with overlapping and competing schemes both at national and local level – a point FSB has made previously⁸⁸. Furthermore, many of the more well-known schemes, such as the former Growth Accelerator programme, have been marketed to 'high-growth' firms, who self-select on this basis. As a result, if they are aware of the existence of such schemes, many self-employed persons may have the impression that they are not suitable for them.

The business support landscape in England is changing, driven by cuts to departmental spending and the need for efficiency savings. Going forward, delivery of enterprise support is increasingly being driven by the private sector or channelled at a local or regional level through Local Enterprise Partnerships (LEPs) and Growth Hubs. As this new look landscape is developed, it is important that relevant schemes and services are targeted at and made relevant for the self-employed, not just SMEs and high-growth firms.

Reflecting the needs of the self-employed should be a priority for the business support offering at all tiers of governance (including mayoral, local authority and LEPs), while the devolved administrations should also ensure its schemes and services are catering for the self-employed. Furthermore, stronger links need to be made to join up local sources of enterprise support (i.e. Growth Hubs) with wider support sought by the self-employed, such as advice on Universal Credit.

Support to those new to self-employment and running a business should also be prioritised. We support the recommendations set out in the Mone review to improve the functioning of the New Enterprise Allowance (NEA) and the support to participants, both pre-claim and once they are on the scheme. This support should be both wide-ranging and targeted to the needs of the individual, and seek to equip self-employed recipients with necessary skills to grow their business.

Beyond the NEA scheme, more can be done to help new business owners and the self-employed obtain the skills they may need to grow their business. As recommended in a recent FSB report⁸⁹, better signposting to online business courses offered by higher education institutions, as well as the creation of 'school for start-ups' programmes run by business schools, could help to widen access to training and provide highly valuable skills to the newly self-employed. Furthermore, recipients of start-

⁸⁶ See <https://www.gov.uk/government/publications/off-payroll-working-in-the-public-sector-reforming-the-intermediaries-legislation>

⁸⁷ Class 2 NICs are being abolished, meaning that the self-employed will only pay class 4 NICs (and as mentioned above, voluntary class 3 NICs to cover any gaps in their NICs record).

⁸⁸ FSB, 'Enterprise 2050: getting UK Enterprise policy right', 2013

⁸⁹ FSB, 'Leading the Way: boosting leadership and management in small firms', 2016

up loans should have the option of using part of their loan to undertake training modules in areas such as leadership and management, thereby equipping themselves with skills that will benefit their business. Tailored support could also be provided to specific groups, such as service leaders and reservists looking to start a business. This should draw on insights from successful initiatives offered in the past, for instance the ‘Be the Boss scheme’ for service leaders which was run by the Royal British Legion and funded by BIS.

Lastly, the Government should take further steps to tackle poor payment practices by commercial clients towards the self-employed and small businesses more widely. The self-employed are often acutely affected by late payment, with freelancers and sole traders suffering most from the imbalance of power in client relationships and a lack of alternative clients to rely on for business. They are also often without the means to seek and obtain redress. The Government should press ahead with plans, currently delayed, to introduce a new ‘duty to report’ on large businesses with regards to their payment terms and practices in order to drive culture change on this critical issue. It should strengthen the remit of the forthcoming Small Business Commissioner, including placing on it an expectation that offending companies will be ‘named and shamed’ where they are found to be at fault (while maintaining the anonymity of the complainant), and also remove from the Prompt Payment Code signatories who repeatedly breach its terms. The Government should also ensure low-cost and accessible commercial dispute resolution services are available for the smallest businesses and the self-employed to enable them to challenge unfair payment practices.

9. Supporting home-based entrepreneurs to grow their business

Finally, with many among the recent ranks of the self-employed running their business from home, the Government should build on recent reforms to support and facilitate home-based working. This trend not only reflects new working patterns and advancements in technology that enables business to be conducted online, but is also a reflection of other developments, including the rising cost of commercial and office premises in many parts of the country.

During the last parliament, the Government introduced several welcome measures to support those who run a business from home. This included amending planning rule guidance to clarify that planning permission to run a business from home is not needed and, similarly with business rates, to state that in most circumstances home-based businesses should not attract business rates. Furthermore, changes to guidance on residential tenancy agreements have made it easier for individuals in rental accommodation to operate their business from home⁹⁰.

Further steps can however be taken and none is more important than broadband connectivity. The Government should prioritise the roll out of high speed broadband to all premises, business and residential, across the country and deliver on its promise of a Universal Service Obligation guaranteeing minimum speeds of 10mbps by 2020 to all premises. It should also task providers to prioritise upload as well as download speeds and set more stretching targets for quality of service agreements, including fault repairs and installation times.

Furthermore, many self-employed, including home-based businesses, benefit from shared work hubs. As recommended in a recent FSB Scotland report⁹¹, local authorities, particularly those in urban areas, should work with other public bodies and private sector partners to ensure adequate provision of shared work spaces, including serviced offices, co-location options and other temporary work spaces. The Deane Review has suggested that local libraries and community centres also have a role in providing these spaces. Consideration should also be given to equipping locations with equipment that is harder to install in the home and to facilitating collaborative working between entrepreneurs.

⁹⁰ See <https://www.gov.uk/government/news/backing-for-home-based-business-boom>

⁹¹ FSB Scotland, ‘Home Truths: The true value of home-based businesses’, 2015

CONCLUSIONS

The growth in self-employment in the UK in recent years has stimulated a significant amount of interest in policy circles, both in terms of understanding the implications for the labour market and the wider economy, as well as whether or not the self-employed are content with working for themselves. This report adds to existing evidence by shedding further light on the profile of the self-employed and the diversity of the self-employed population, as well as the benefits and challenges of self-employment.

In this report, we have focused on improving understanding of the personal challenges faced by the self-employed, such as income volatility, putting aside savings and financial inclusion. We suggest - as other reports have done also - that these areas should be priorities for policymakers in the coming years. Alongside this, Government should continue to enact reforms in other areas that are beyond the scope of this report, such as providing high-quality enterprise education in schools in order to spark interest among young people in business at an early age, so that they may become the business leaders of the future.

What appears certain is that high levels of self-employment are here to stay and policymakers need to ensure all aspects of Government policy recognise this and are geared towards the self-employed. Supporting those that go it alone, and helping the self-employed succeed, will be crucial for maintaining a strong labour market and delivering the dynamic and enterprising economy of tomorrow.

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