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ARE YOU BUYING PEOPLE OR BUYING SERVICES?

The sourcing question at the heart of commercial and tax risk



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AT A GLANCE

Organisations are increasingly using external providers to access specialist skills and surge support, accelerate transformation and deliver operational outcomes. As delivery models become more flexible, the distinction between buying a service and buying people is becoming harder to draw.

That distinction now matters well beyond Procurement. It can influence workforce governance, tax and legal obligations, supply chain risk and access to innovation incentives. None of this means that Procurement or Supply Chain teams should become tax specialists, or that tax advisers should become Procurement professionals. However, the distinction between buying services and buying people sits squarely at the intersection of commercial decision-making and tax risk, where shared governance across these disciplines can deliver significant long-term value.

Across sectors, businesses are adopting more sophisticated sourcing models. Some are retaining accountability for delivery while using external specialists to supplement internal teams. Others are outsourcing defined operational outcomes through managed service arrangements. Many relationships sit somewhere between those two models and evolve over time.

This evolution can make it difficult for the contractual description of an arrangement to reflect what is actually being delivered, and how the arrangement operates in practice may not align with the contract. A contract may describe consultancy or outsourced services, while the operational reality is long-term access to named specialists embedded within client teams.

UK tax and regulatory regimes increasingly look through contractual labels and focus on commercial substance. That makes it important for Procurement, Legal, HR, Finance and Tax teams to understand what is being bought and how supplier services are delivered in practice. The answer is not always clear cut.

Procurement has a critical role to play: not by becoming tax specialists, but by asking the right questions early, testing whether the arrangement is truly people or services, and knowing when to bring the right expertise to the table. Deloitte brings together Procurement, Supply Chain, Tax, Legal, Workforce and Consulting Managed Solution specialists to help organisations design compliant, commercially effective models that keep pace with evolving supplier relationships.

1 WHY THE QUESTION IS BECOMING MORE IMPORTANT

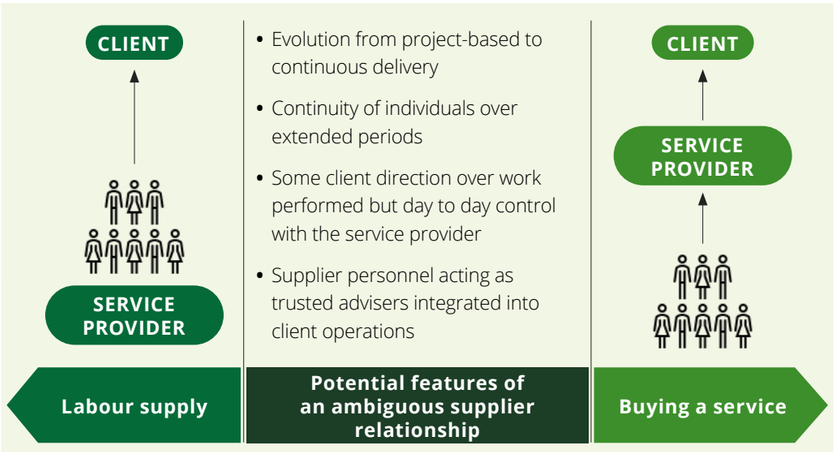
The distinction between buying people and buying services is not new. Procurement teams have always chosen between outsourcing defined outcomes, engaging professional services, accessing specialist capability and supplementing internal teams.

What is changing is the environment in which those decisions are being made. Across almost every sector, organisations are under pressure to deliver technology transformation more quickly, modernise legacy platforms, respond to changing customer expectations and regulatory pressures, and adopt emerging technologies such as artificial intelligence. At the same time, many continue to face cost pressure and intense competition for scarce specialist skills.

These forces are changing not only what organisations buy, but how they buy it. Rather than defaulting to a single sourcing model, businesses are becoming more selective about where they want suppliers to deliver defined outcomes and where they need access to specialist or scale capability. In practice, this means the boundary between an outsourced service and the supply of people is becoming less clear.

The trend is not consistent across every industry. Different sectors are making different choices depending on the nature of the work, the maturity of their technology landscape, the availability of talent and the commercial outcomes they are trying to achieve.

Understanding the arrangement: A simple illustration of the spectrum between labour supply and service provision. While some arrangements fall clearly at either end, many combine characteristics of both models, creating ambiguity and uncertainty.





2 | HOW DELIVERY MODELS ARE EVOLVING ACROSS SECTORS



The commercial drivers differ by sector, but the underlying challenge is similar: organisations need to understand whether they are buying an accountable service, accessing specialist capability, or operating a hybrid model that may evolve over time.

Banking: retaining ownership, accessing expertise

Many financial institutions appear to be changing the way they access emerging talent and consume external technology services. While major transformation programmes continue to involve consulting firms and systems integrators, many banks are increasingly investing in their own engineering capability and using external providers to supplement scarce specialist skills rather than to lead entire programmes.

This is particularly evident in areas such as cloud engineering, cyber security, platform architecture, data engineering and artificial intelligence. Several factors appear to be driving this shift. Technology has become a strategic differentiator, making it increasingly attractive to retain intellectual property and technical knowledge within the organisation. Agile delivery models also favour integrated product teams, where external specialists work alongside permanent employees rather than operating independently. Organisations also require new talent to hit the ground running in integrated technology and operations teams, often favouring a 'hire-train-deploy' model to access emerging talent who have already bridged the gap between education and employment. Furthermore, they can benefit from gaining a 'try-before-you-buy' perspective on new joiners, mitigating the risk to permanent roles by proving potential new hires before commitment.

The consequence is that Procurement is often buying access to specialist capability rather than outsourcing responsibility for delivery.

Insurance: buying operational outcomes

Insurance organisations often face a different commercial challenge. Many continue to modernise complex legacy estates while simultaneously seeking operational efficiencies and lower cost-to-serve. In this environment, outsourced services remain an attractive delivery model because they enable organisations to transfer responsibility for defined operational outcomes while allowing suppliers to introduce automation, process improvements and technology investment. Whether supporting claims operations, infrastructure management or application support, insurers frequently seek suppliers that assume accountability for ongoing service delivery rather than simply providing additional resource.

Specialist capability is still required for major transformation programmes and high-value operational tasks, but there often remains a clearer distinction between buying expertise and buying an operational outcome.

Energy Trading: when capability becomes the service

Energy Trading businesses present a particularly interesting example. Specialist expertise in Energy Trading and Risk Management (ETRM) platforms, quantitative development, trading technology and real-time market infrastructure is both commercially critical and relatively scarce. For many organisations, accessing these skills through external providers is not simply a matter of flexibility; it is often the only practical way to secure the capability required.

As a result, supplier personnel frequently work alongside traders, quantitative analysts, market risk teams and internal technology functions over extended periods. The engagement may begin with a clearly defined implementation project. Over time, however, the work can evolve into continuous platform enhancement, regulatory change and product development. The supplier remains the same. Many of the individuals remain the same. The delivery model, however, may have evolved significantly. Commercially, the arrangement may still be described as consultancy but operationally, it increasingly resembles access to highly specialised capability embedded within the organisation.

Similarly, dependency on legacy platforms and delays in transformation or migration can result in organisations having diminishing access to internal skills as the labour market moves on. Third parties can help organisations overcome these shortages through direct augmentation, as well as offering the flexibility to access business-as-usual backfill support at the point of need, to shore up increasingly critical internal roles.

Technology: specialist capability at speed

Technology businesses have long relied upon a blend of permanent employees and external specialists. What appears to be changing is the increasing demand for highly specialised expertise in areas such as AI, cloud platforms, cyber security and data engineering. Rather than engaging large consulting teams, organisations often seek smaller specialist providers capable of integrating rapidly into product teams and accelerating delivery. These engagements often combine elements of consultancy, professional services and resource augmentation, making it increasingly important to understand the commercial substance of the arrangement rather than relying solely on contractual terminology.

Public Sector: regulation influencing delivery models

The Public Sector provides another perspective. Government departments and public bodies continue to rely upon a mix of outsourced services, systems integrators and specialist resources to deliver complex transformation programmes. However, changes in legislation, particularly the extension of the off-payroll working rules to the Public Sector, have also influenced how organisations procure external capability. In addition, the use of procurement frameworks within the Public Sector can create further complexity, particularly where it is unclear whether what is being procured is a service or access to people.

This demonstrates an important point. Delivery models are shaped not only by commercial considerations but also by the wider regulatory and procurement environment in which organisations operate.

A common thread

Although the commercial drivers differ across sectors, a common theme is emerging. The distinction between buying a service and buying people is becoming less obvious and governance established in response to tax legislation (including IR35) should be re-evaluated. In some sectors, organisations increasingly seek specialist capability while retaining responsibility for delivery. In others, they continue to favour outsourced services that transfer accountability to the supplier. Many organisations operate somewhere between those two models, with delivery evolving as programmes mature. Indeed, we occasionally see requests for staffing of programmes which seek to leverage more than one preferred supplier list (PSL) concurrently, for instance combining both Management Consultancy and Augmentation demand within a single delivery, with roles distributed across specialisms and the segregation of complexity. None of these approaches is inherently better than another. The important point is that different delivery models create different commercial relationships, and can also affect tax and legal responsibilities and opportunities.

3 WHEN SERVICES BECOME PEOPLE: WHY COMMERCIAL SUBSTANCE MATTERS



One of the defining characteristics of modern delivery models is that they evolve. At the outset of a procurement exercise, organisations are generally clear about what they are buying. A statement of work is agreed, responsibilities are allocated and commercial terms are negotiated on the basis of an agreed delivery model.

The supplier may be appointed to deliver a defined outcome, implement a technology platform or provide specialist expertise over a fixed period. However, projects rarely stand still. Business priorities change. Technology evolves. Delivery approaches become more agile. Relationships mature. Supplier personnel become trusted advisers because they understand the organisation, its systems and its strategic objectives. In many respects, this is exactly what organisations hope will happen.

Successful transformation programmes are built on collaboration, continuity and shared understanding. The challenge is that the commercial relationship often evolves without anyone consciously recognising that it has changed.



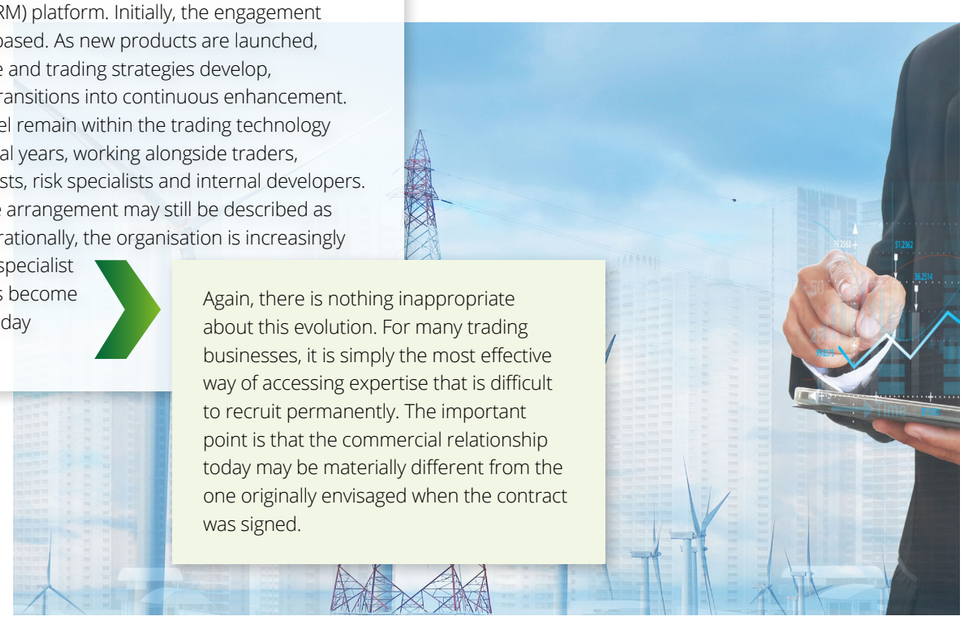
The contract stays the same; the delivery model changes



Consider a global investment bank embarking on a multi-year cloud transformation. Initially, the bank appoints a systems integrator under a statement of work to deliver a defined migration programme. The supplier is responsible for planning, delivery, governance and resource management. Success is measured by agreed milestones and programme outcomes. Eighteen months later, the programme looks very different. The migration has become continuous platform development. Supplier engineers attend daily stand-ups alongside bank employees. Product owners prioritise work directly with integrated delivery teams. The same specialists remain embedded within engineering squads because their knowledge of the platform has become commercially valuable.

Nothing has gone wrong. Indeed, the programme may be more successful because of this evolution. However, the nature of the relationship has changed. What began as the procurement of an outsourced service increasingly resembles access to specialist engineering capability embedded within the organisation. The contract may remain largely unchanged. The commercial substance of the arrangement has not.

A similar pattern can often be seen within energy trading organisations. A specialist consultancy is appointed to implement or enhance an Energy Trading and Risk Management (ETRM) platform. Initially, the engagement is clearly project-based. As new products are launched, regulations evolve and trading strategies develop, implementation transitions into continuous enhancement. Supplier personnel remain within the trading technology function for several years, working alongside traders, quantitative analysts, risk specialists and internal developers. Commercially, the arrangement may still be described as consultancy. Operationally, the organisation is increasingly accessing scarce specialist capability that has become integral to day-to-day operations.



Again, there is nothing inappropriate about this evolution. For many trading businesses, it is simply the most effective way of accessing expertise that is difficult to recruit permanently. The important point is that the commercial relationship today may be materially different from the one originally envisaged when the contract was signed.



4 COMMERCIAL SUBSTANCE DRIVES TAX OUTCOMES

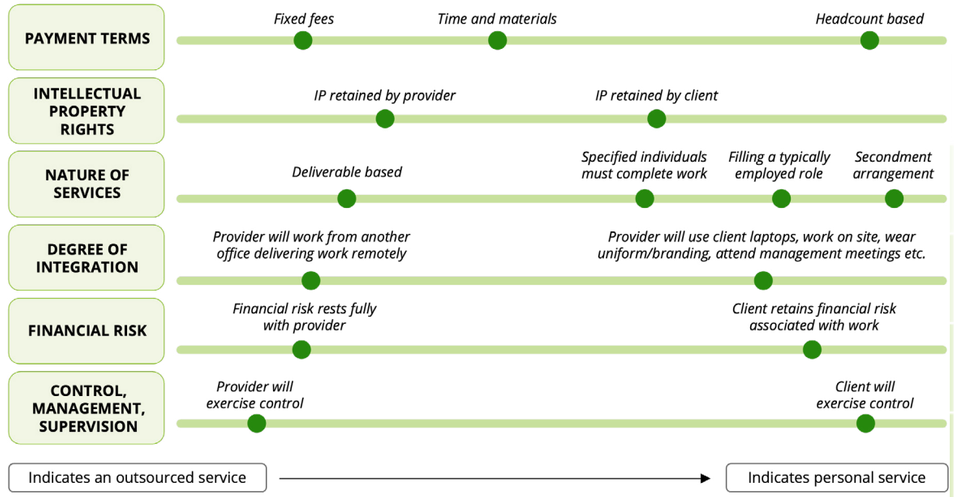
One of the enduring principles underpinning much of UK tax legislation is that substance prevails over form. The same principle is relevant to procurement contracts and to assessing whether the underlying relationship is a service arrangement or a supply of people. This matters for tax and legal purposes.

Whether considering the off-payroll working rules, the UK's umbrella company rules, agency legislation or aspects of the R&D tax relief regime, the outcome often depends on the true commercial nature of the relationship and what happens in practice, in addition to considering the contractual terms and obligations imposed on the parties to the contract.

That does not mean organisations should avoid resource augmentation or outsourced services. Both remain important and commercially valuable delivery models. The challenge is ensuring that the commercial model being operated is understood, appropriately documented and periodically reassessed as delivery evolves.

Increasingly, it is the commercial substance of the arrangement, not simply its contractual label, that determines the tax outcomes that follow.

Making the distinction: A simple matrix of factors providing indicators of an outsourced or a personal service. In practice, making the distinction can be much more nuanced and requires detailed assessment.



5 KEY TAX & LEGAL AREAS



Off-payroll working – IR35

Deciding whether a contract is for people or services is the gateway test that determines whether the supplier or its client is legally responsible for evaluating IR35 tax obligations. For Procurement and Supply Chain teams, this may be an unfamiliar concept, but Finance and Tax specialists will recognise that it can be a key component of an organisation's tax risk profile.

An organisation receiving a service does not have to comply with IR35 rules. The practical issue is the risk of getting the 'service or people' distinction wrong. We have seen suppliers present a services model that is staffed by off-payroll subcontracted resource via Personal Service Companies. Treating that resource as 'outside IR35' can reduce the supplier's delivery cost, including 15% employer NIC, and may make the supplier more competitive at tender. However, if HMRC later successfully contests that the arrangement was a supply of people, the supplier's client may be liable for taxes and penalties. Contracts often contain carefully worded indemnities, but these do not prevent HMRC pursuing the supplier's client and, in our experience, would rarely be invoked.

Umbrella company supply chains

From 6 April 2026, new PAYE rules introduce joint and several liability risk into labour supply chains. A common misconception is that the rules apply only to traditional umbrella companies, meaning entities whose business is primarily to payroll and employ people who then work for a range of clients on a temporary basis. In fact, the rules apply more broadly to organisations that supply people, and can include traditional consultancies, where they use labour augmentation or secondment models alongside outsourced arrangements. For organisations procuring a service, the new joint and several liability rules should not apply. They are more likely to apply to consultancies supplying people, which can in turn affect their clients. This makes it important to include contractual provisions that clearly allocate obligations and provide appropriate protections.

This also mirrors the longstanding risk of VAT fraud arising in labour supply chains, particularly those involving "mini umbrella companies", which can give rise to serious civil and criminal consequences for organisations that "knew or should have known" of fraud within those supply chains. In recent years, this has become a key area of focus for HMRC, and it is important that organisations carry out robust due diligence before entering into such arrangements. HMRC's Guidelines for Compliance 12 provides a useful starting point for establishing good practice in this area.

R&D tax relief

The distinction between buying people and buying services can also affect R&D tax relief. Where the contract is a supply of people, broadly meaning that the workers operate under the client organisation's supervision, direction or control in a manner comparable to its own employees, HMRC treats them as "Externally Provided Workers" (EPWs), and 65% of the amounts paid to the supplier can qualify as R&D expenditure for tax relief purposes. However, where the arrangement is structured as a supply of services, with the external provider determining how the work is performed and retaining control over delivery, it falls under subcontracting rules instead, which carry different conditions. For Procurement and Supply Chain teams, this means that the wording of contracts, the day-to-day management of workers, the allocation of economic risk and reward, and who directs how tasks are carried out all matter. Getting this wrong at the procurement stage can significantly impact the tax relief an organisation is entitled to claim, or expose it to challenge by HMRC. Procurement and Supply Chain specialists should therefore engage their tax team early when evaluating these arrangements.

Value Added Tax

The VAT treatment of supplies in this area can differ depending on a number of factors, including:

- Whether there is a supply of staff or a supply of the services performed by those staff; and/or
- Which payments fall within the consideration subject to VAT (for example, payments to workers).

Importantly, services between employer and employee (in the course of their employment) fall outside the scope of VAT.

A supply of staff is usually (noting there are some exceptions) subject to VAT at the standard rate, regardless of the nature of the supplying business. By contrast, where the supplying party is instead providing services, for example, medical, care or construction services, that is not a supply of staff but a supply of those services. Depending on their nature, such services may be subject to various different VAT treatments. The VAT treatment of arrangements in this area therefore turns on two consequential questions:

- Whether the arrangement constitutes a supply of staff, which is typically subject to VAT at the standard rate, or a supply of the services performed by those staff, which may follow a range of different VAT treatments; and
- In the case of a supply of staff, correctly identifying which payments are deemed to fall within the taxable consideration subject to VAT.

Some businesses may be able to recover all of the VAT charged by suppliers, although it remains important to recover VAT on the correct amount. However, the distinction between a supply of staff and a supply of their services can be most consequential for organisations operating in partially exempt sectors, most notably Health, Education or Financial Services, where irrecoverable VAT on purchases from suppliers usually represents a hard cost.

HMRC will often challenge arrangements where it considers that the contractual description does not reflect the underlying substance. For example, where the reality is that staff are being supplied and directed and controlled by the recipient, but the contract presents the arrangement as services, or vice versa, HMRC may seek to apply a different VAT treatment. Importantly, the contractual structure is not the sole determining factor; HMRC and the tribunals will look at the substance of the arrangement, in particular the question of direction and control. This risk is compounded in arrangements that evolve over time, where the VAT analysis performed at the outset may no longer reflect how the arrangement operates in practice. Noting the significant body of VAT case law on this topic, it is important to revisit existing arrangements and consider the potential VAT impact.



Employment Law

While the tax implications of the people versus services distinction receive significant attention, the employment law consequences are equally important and can arise independently of the tax analysis. An individual who is treated as self-employed for tax purposes may nonetheless be found to have worker or employee status for employment law purposes, each carrying distinct statutory entitlements. Employment tribunals assess status by reference to the underlying reality of the relationship in addition to its contractual description, and a finding of worker or employee status can give rise to backdated claims for holiday pay, pension auto-enrolment contributions and National Minimum Wage arrears.

This risk is most acute where supplier personnel are embedded within a client organisation over an extended period, operating under day-to-day client direction and integrated into its teams. Where such claims arise at scale across a large supplier programme, the financial and reputational exposure can be material.

Separately, where supplier personnel are in substance supplied through an agency arrangement, the Agency Workers Regulations 2010 may entitle those individuals to equal treatment with comparable directly employed staff after a twelve-week qualifying period, regardless of how the contractual arrangement is described.

Organisations should also be aware that the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE) may apply where a managed service arrangement transfers from one supplier to another or is brought in-house. Where the commercial reality is that an organised grouping of employees is dedicated to a particular client's activities, a TUPE transfer may be triggered, with the result that the contracts of employment of affected employees transfer automatically to the new employer by operation of law together with all associated rights and liabilities.

The Employment Rights Act 2025 further heightens these risks. The reduction of the unfair dismissal qualifying period from two years to six months increases the exposure where embedded individuals are later found to have employee status. New rights for workers on zero-hours and low-hours contracts, including guaranteed hours and compensation for late shift cancellation, may also be relevant where supplier personnel are engaged on flexible arrangements.

Contracts, statements of work and day-to-day governance should reflect the commercial substance of the arrangement and be kept under review as that substance and the legislative landscape evolve.



Immigration

The people versus services distinction has direct consequences for Right to Work ("RTW") compliance in the UK, an area undergoing significant change from 1 October 2026.

Under the existing framework, the obligation to conduct a RTW check, and the associated civil penalty liability for employing individuals without valid immigration status, attaches to the employer that holds a direct contract with the worker. Where a client organisation procures a genuine outsourced service, responsibility sits with the supplier, not the client. The risk is most acute where arrangements that are documented as service contracts operate in practice as a supply of people.

From 1 October 2026, new regulations extend both RTW obligations and civil penalty liability up the contractual chain. Where a contractor is engaged to provide work or services and that work is personally delivered through a chain of sub-contracts, the organisation at the top of that chain may be treated as the employer of the individual providing the work, even where there is no direct contractual relationship with that individual. Importantly, the extended liability provisions are expected to apply broadly. In particular, arrangements involving substitution clauses as well as those where an online platform is used to procure labour or services, are likely to fall within the scope of extended liability under the new regulations.

Consider, for example, a professional services firm that relies on a chain of subcontracts to fulfil its delivery obligations to a UK corporate. The subcontractors and staffing vendors would be responsible for conducting the RTW check on workers supplied to the professional services firm. However, the subcontracting arrangements between the professional services firm and those subcontractors fall within the extended liability provisions. This means that liability can reach further up the contractual chain, notwithstanding the fact that the UK corporate does not hold a direct contract with the worker. The organisation must therefore also maintain systems to verify that the individual attending to perform the work is the same person whose right to work was checked, which in practice requires conducting an identity document check against the original RTW check (called an identity check).

It is possible to qualify for a statutory excuse where extended liability applies, removing the need for an organisation to conduct a RTW check itself. To do so, however, it must ensure that its supplier and sub-contractor contracts contain prescribed provisions, including requirements to conduct RTW checks on all workers delivering the contract, restrictions on further sub-contracting without consent, obligations to cooperate with any Home Office investigation and obligations to carry out identity checks.

As with employment law and tax, contractual substance matters. Arrangements that are described as service contracts but operate as a supply of people may not attract the protections available to genuine outsourced service clients and could expose the client to civil penalty liability it had not anticipated. Procurement, legal and HR teams should consult an immigration specialist and carry out an immigration compliance health check to identify and manage any existing risk and to ensure that adequate processes and policies are in place. Supply chain arrangements should also be reviewed in light of the October 2026 changes to ensure that appropriate contractual protections are established before the new rules take effect. Finally, the use of digital verification technology, such as Deloitte's Go Verify tool, is becoming highly advisable in this increasingly complex area and organisations should consider adoption to support this process.



6 WHAT ORGANISATIONS SHOULD DO NOW: A SHARED GOVERNANCE RESPONSIBILITY

The most effective organisations increasingly recognise that Procurement, Legal, HR, Finance and Tax all have a role in understanding how external capability is acquired and how delivery models evolve over time. The objective is not to favour one sourcing model over another. It is to ensure that the commercial substance of the arrangement remains consistent with the way services are actually delivered in practice. Organisations should:

1. Map strategic supplier and workforce arrangements involving consultancy, outsourced services, resource augmentation and specialist technology delivery.
2. Identify arrangements where delivery has evolved since the contract was signed, particularly where supplier personnel are embedded within client teams.
3. Assess whether contracts, statements of work and operating practices tell a consistent story.
4. Review labour supply chains to understand whether umbrella companies or similar third parties are involved.
5. Bring Procurement, Legal, HR, Finance and Tax together to agree clear ownership for ongoing governance.
6. Consider tax, legal and regulatory consequences before renewing, extending or materially changing supplier arrangements.
7. Review the impact of recent legislative changes, such as the umbrella company rules (implemented 6 April 2026), and future anticipated changes, for example the Right to Work changes (expected 1 October 2026) to assess impact and ensure readiness.

Deloitte has extensive experience of both supporting organisations in evaluating the 'people' versus 'services' dynamic across sectors, and providing compliant-by-design people and services models. We draw on our network of Procurement, Tax, Legal, Workforce and Consulting Managed Solution experts, to optimise how you access specialist skills and surge support, accelerate transformation and deliver your world-class operational outcomes, whilst continually monitoring and navigating these complexities.

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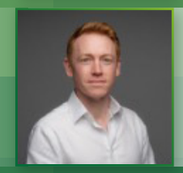
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