TACKLING DISGUISED REMUNERATION

ICAEW welcomes the opportunity to comment on the technical consultation document *Tackling disguised remuneration* published by HMRC on 10 August 2016.

The timing of this consultation document, issued in a similar timeframe to about thirty other papers seeking comments, has restricted the time we have been able to spend on this response.

This response of 7 October 2016 has been prepared on behalf of ICAEW by the Tax Faculty. Internationally recognised as a source of expertise, the Faculty is a leading authority on taxation. It is responsible for making submissions to tax authorities on behalf of ICAEW and does this with support from over 130 volunteers, many of whom are well-known names in the tax world. Appendix 1 sets out the ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark proposals for changes to the tax system.

We should be happy to discuss any aspect of our comments and to take part in all further consultations on this area.

On 3 October 2016 we attended a meeting with HMRC in which we were able to put forward some key comments and concerns and discuss aspects of the consultation document.

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The Institute of Chartered Accountants in England and Wales
Chartered Accountants' Hall
Moorgate Place London EC2R 6EA UK
icaew.com/taxfac

T +44 (0)20 7920 8646
F +44 (0)20 7920 0547
E taxfac@icaew.com

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ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.

For more information, please contact ICAEW Tax Faculty: taxfac@icaew.com

icaew.com

GENERAL COMMENTS

1. We are very concerned about the proposals in the consultation document as they contravene generally accepted notions of fairness and break the constitutional convention against retrospective legislation, imposing tax charges in cases where taxpayers already had legal certainty that none were due.

2. The proposed 2019 loan charge also seems at variance with HMRC's arguments in many cases (successful to date) that monies paid via employee benefit trusts (EBTs) and employer funded retirement benefit schemes (EFRBS) were actually earnings that should have been subject to PAYE and NIC. It makes it unclear whether the loans are loans or earnings, which offends against the second – Certainty – of our *Ten Tenets for a Better Tax System*, summarised in Appendix 1.

3. The proposals are aggressively retroactive against taxpayers who have not done anything that would under current rules leave themselves open to a 20 year assessing window which currently requires HMRC to demonstrate that there has been a deliberate inaccuracy in a return. Where there is an enquiry into tax suspected to have been evaded or deliberately misstated, then going back to 1999 is permissible under the 20 years rule. However it is not acceptable for HMRC to create a retrospective tax liability where none currently exists, especially as HMRC has been aware of loans to employees (referred to in the consultation document – and adopted here for convenience only – as disguised remuneration (DR) schemes) since at least 1999 and has failed to open inquiries or raise assessments before the expiry of statutory deadlines. Using retrospective legislation to remedy lacunae in HMRC's procedures is unreasonable.

4. Under the legislation as it presently stands, Parliament allows HMRC to assess six years in cases of careless (as opposed to deliberate) error, provided HMRC takes action within that six year window. Few, if any, of those taxpayers involved in DR schemes will have filed inaccurate returns, either carelessly or deliberately, so HMRC should arguably be limited to assessing events only in the last four years. The proposed legislation will extend this in 2019 to 20 years including years that are 'closed'. To introduce legislation which affects transactions which were entered into up to 17 years ago (measured from the current year) where HMRC has taken no timeous action despite knowledge of the alleged avoidance is likely to lay the proposed legislation open to challenges under the Human Rights Act.

5. Given that those involved in DR arrangements will have disclosed the transactions that they entered into, we are also surprised at the contrast between the favourable terms given to so-called tax evaders under the former Liechtenstein Disclosure Facility and what is proposed for DR in the consultation document.

6. It appears that the consultation does not recognise the fact explicitly that some taxpayers who took the option of not receiving a corporation tax deduction in the recent EFRBS Resolution Opportunity could also be subject to the loan charge in full. We should welcome confirmation that there will be no income tax or NIC charge in these cases, as implied at paragraph 40 of Chapter 4. Should such confirmation not be given, we should welcome confirmation that credit is given for any corporation tax paid under the resolution opportunity against the income tax and NIC due under a subsequent and wholly inequitable loan charge.

7. Many of the outstanding cases are already covered by existing legislation, in particular the s.554A gateway. HMRC should apply existing legislation rather than giving the impression of being unable to take action by proposing new legislation duplicating what is already there.

8. On the international scene these proposals when considered in the light of other recent and proposed changes to employer taxes and payroll, benefits-in-kind and expenses reporting processes are making the UK appear a more 'difficult' country in which to locate staff, which may not be desirable in today's fragile economic climate.

SPECIFIC COMMENTS

Chapter 2: Tackling the continued use of schemes

9. In paragraph 26, we question HMRC's starting premise. Parliament has long accepted that a business that pays remuneration should receive a deduction. Deferral of that deduction is a fair disincentive to paying remuneration via a third party. Denial of a deduction is a disguised penalty.

Chapter 3: Transfer of liability

10. In paragraph 13, we should welcome clarification of how a worker is to know whether or not the UK user is accounting correctly for liabilities under s.689. The rules seem likely to catch some situations that do not simply involve one-man companies where the flow of untaxed cash is clear.

11. In paragraph 14, there seems to be some confusion between avoidance schemes and evasion, such as deliberately using and liquidating a company with no intention of ever paying the taxes due. Again, where there is evasion, HMRC would seem to already have the necessary means to pursue the alleged arrears without extra legislation.

12. In paragraphs 20 and 21, HMRC would surely need, despite its arguments to date in EBT loan cases, to abandon all claims that loans were earnings before being able to convince a tribunal to assent to a transfer of liability. Does this paradox not undermine the proposals fundamentally?

Chapter 4: The loan charge

13. As noted under General Comments we are concerned about the retrospection of these provisions.

14. In paragraphs 2 to 4, the close company gateway adds nothing to the s.554A gateway which effectively covers every situation and risks creating a DR charge where there is no link between the payment and an employment in certain circumstances (eg, where the company is owned by a family trust related in some way to the future, current or former employee).

15. In paragraph 6, we question why a replacement loan should fall within the legislation when it is essentially the same loan as the original.

16. In paragraph 10, we should welcome clarification of why HMRC considers that regulation 72 of the PAYE regulations is not applicable; our understanding is that the UK entity is 'standing in the shoes' of the employer under s.689.

17. In Example 4.9, if 'A' wins the litigation, there is surely no DR scheme loan. We should welcome clarification of why A should then have to repay the loan, which has been proven in court not to be offensive to tax law.

18. In paragraphs 38 to 41, under the previously offered settlements, either the PAYE income tax and NIC could be paid and the structure unwound, or the employer would pay the corporation tax and leave the structure. Under the proposals, it appears that no credit is given for corporation tax paid, so employers will incur charges to both corporation tax and PAYE/NIC. This is double taxation, and, in effect, a penalty for using a tax scheme that was legal at the time the transactions were undertaken. We note that the 60% GAAR penalty is not going to apply retrospectively, and we question whether by comparison the proposal is fair or just. We consider that in the interests of fairness only one of the taxes should be payable.

19. We should welcome clarification of how the proposed changes interact with the IHT legislation that will apply to payments out of the typical DR trust arrangements.

APPENDIX 1

ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.

2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.

3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.

4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.

5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.

6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.

7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.

8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.

9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.

10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see via http://www.icaew.com/en/about-icaew/what-we-do/technical-releases/tax).