BRINGING FREELANCERS TOGETHER

Financial Secretary, Jesse Norman, writes to MPs

The Loan Charge Action Group is aware that Jesse Norman MP, the Loan Charge Minister, recently wrote to Conservative colleagues regarding the Loan Charge.

Mr Norman claims that he was seeking to clarify certain aspects of this legislation when in fact he was merely trying to justify if with further spin and misleading statements.

We would like to set straight some of the mistruths in Mr Norman's letter, which we have done below. The following text in **black** is Mr Norman's original letter, with responses from LCAG in **red** text.

<u>The Loan Charge</u>

The Loan Charge was announced at Budget 2016 and passed into legislation in Finance Act (no. 2) 2017. It is designed to collect tax due on disguised remuneration tax avoidance schemes; more than 250 such schemes have been identified by HMRC. The Supreme Court found the most well-known scheme used by Rangers Football Club, and schemes similar to it, to be ineffective in law. The Government and HMRC repeatedly encouraged those who had used disguised remuneration schemes to come forward by 5 April 2019, when the Loan Charge came into force.

In the Rangers Case HMRC tried to argue that loans were taxable. The Courts found otherwise, they ruled that the loans were "*not a sham*" and therefore not taxable. This is precisely the ruling that the Loan Charge - in conjunction with its "voluntary settlement" partner - attempts to subvert.

Jesse Norman is misrepresenting this ruling to suggest it offers legal justification for the Loan Charge. **It doesn't.** What the judgement actually ruled was that payments from employers into EBTs were taxable. This is a matter that falls under standard (and existing) PAYE rules and the Taxes Management Act 1970.

The Supreme Court ruling was made in 2017. The Loan Charge is retrospective to 1999.

No other arguments or arrangements were adjudicated on by the Supreme Court.

To say HMRC's idea of "repeated encouragement" is low key would be an understatement. Their strategy has been one of publishing opinion in Spotlight articles that only Tax professionals would ever review and sending letters to a few people they suspect of being involved. Regarding the Loan Charge, HMRC only started sending direct mail notices to people in May 2018 and then only in small volume. Many people have yet to receive any notification of the Loan Charge.

Disguised remuneration tax avoidance

In a typical disguised remuneration scheme, an offshore trust is used to channel income to individuals in the form of a loan, which gets bigger each time the individual is paid.

Unlike normal loans, disguised remuneration loans are generally provided interest-free, without a schedule of repayments of the capital, and without any date for repayment. No assessment is made of the creditworthiness of the individual before the loan is made, and no security is sought against failure to repay. Individuals are not pursued for failure to repay the loan, there is no expectation that the loan will ever be repaid, and in practice the loan is not repaid. Thus, these are highly contrived arrangements.

Mr Norman's opinion on the contrivance of these arrangements is both irrelevant and arguable. The Supreme Court decision still agrees that these were genuine loans. It is the law that is important in tax cases and HMRC have repeatedly been told in various courts that 'loans are loans'.

Typically, the individual is also paid a salary set below the level of the personal allowance, but still qualifying for the state pension.

It is claimed that this arrangement results in little, or no, income tax and employee National Insurance contributions being due on the payments received. The de facto employing company does not pay full employer National Insurance contributions, and often claims a deduction in their accounts for the payments made.

The returns to the individual from loan arrangements were similar to the net income of a contractor working through their own PSC. The promoters of loan arrangements deducted large fees with the individuals being assured that the correct taxes had been paid.

Since 2004 promoters have been required by law to provide a Disclosure of Tax Avoidance Scheme reference number to their clients. Some promoters even asked individuals to contribute to funds to fight the expected HMRC challenge to the schemes through litigation.

This is not factually correct. HMRC have changed their guidance on this over the past few years, and whilst the guidance now says that the reference number has to be provided this was not always the case – and not all arrangements required

a DOTAS number. If HMRC guidance changes then it is difficult to see how non-tax professionals are supposed to know what action they should take.

Where DOTAS numbers were issued, the promoters often used them as evidence that the arrangements were approved by HMRC. Combined with HMRC's failure to open enquiries into many years where a DOTAS number was on the person's tax return, this belief is understandable.

Any of the features above could have indicated to someone that they were benefitting from tax avoidance. Many people recognised this and declined to enter into these schemes.

Tax avoidance is legal. HMT and HMRC have tried to paint this in a very different light by conflating avoidance with evasion and creating a public perception that someone avoiding tax is a criminal. This can be seen in their recent mission statement which contains the purposely conflated phrase "bear down on avoidance and evasion".

There is also an assumed degree of financial knowledge on the minister's behalf; nurses, doctors, teachers and other contractors using these arrangements may be experts in their own fields but have little knowledge of tax law. For many this was the reason for using schemes. They were mass marketed by big companies over many years so it would be assumed by the layperson to accept them as valid.

The position of the Government and HMRC has always been that disguised remuneration schemes do not avoid tax due. Parliamentary statements on tax avoidance schemes go back to 2004, when the then Paymaster General made clear that the tax payable would be collected. HMRC have opened tens of thousands of enquires into users of these schemes, with the first cases being opened before 1999.

The government's position stated here is irrelevant. Whispers in HMRC or speeches to Commons Committees are not law and certainly do not reach the average taxpayer. The only subject of concern is the law, as decreed by Parliament and confirmed by the courts. HMRC suffered repeated losses in court trying to prove that tax is due on a loan. As previously stated even the Supreme Court decided that loans were not taxable.

Regardless of the number of enquiries opened, it stands to reason that HMRC have also failed to open hundreds of thousands of enquiries. Taxpayers should be entitled to certainty in their affairs. The Tax Management Act puts statutory time limits for exactly this reason. The Loan Charge was designed to specifically remove these rights and protections.

From the enquiries that have been opened, HMRC have never been successful in proving that any tax is due from the individual. In numerous cases enquiries were opened many years ago (sometimes up to 20 years ago) yet the individual is still to hear from HMRC on the progress of that enquiry. These enquiries should now be closed as they are dormant. Recent case law endorses the fact

that many of these will now be considered as 'stale' and that HMRC are simply out of time.

HMRC are also committed to challenging tax avoidance promoters and have over 100 under investigation. HMRC are doubling the resources devoted to this work. This includes identifying, challenging and pursuing in court scheme promoters, as well as using communications to disrupt and deter promotion activity.

Why are they under investigation? The minister admitted during a session of the Lords Economic Affairs Committee on 16th July 2019 that promoters of contractor loan arrangements had done nothing illegal and that pursuing them would require a **retrospective law** and that would be **against the law**. Should it not then follow that people who simply signed up to these marketed payroll schemes should also be free from retrospective laws? Why then have the government decided to retrospectively and punitively target individuals with the Loan Charge? The answer is perhaps very simple; because they are seen as the easier targets?

More than 99.8 per cent of taxpayers do not use disguised remuneration schemes. It is unfair that a very small minority are seeking to avoid paying tax here.

HMRC have a duty to treat all taxpayers fairly and equally. Stating that a percentage of taxpayers have not used a contractor loan arrangement is totally irrelevant.

Listening to stakeholders

There has been a considerable amount of misinformation in relation to the Loan Charge, which has caused confusion and anxiety among those affected. However, there are also some genuine concerns, which need to be addressed.

It is ironic that the minister refers to misinformation regarding the Loan Charge, when much of it has come from the Treasury and HMRC themselves. Examples include clearly misleading statistics and the misrepresentation of action taken by HMRC. As a clear example, HMT and HMRC made many public statements about how there had been six arrests related to loan schemes. In reality they had arrested alleged fraudsters who were trying to con people into paying for a solution to evade the Loan Charge.

Another example would be the way that HMRC have publicised the outcome of the Hyrax case, saying that it was a win against a tax avoidance scheme. The fact is that it was a case where the outcome was about the requirement for DOTAS registration and absolutely nothing about the actual arrangement itself.

Specifically, these include concerns that the policy may breach established norms of taxation by reopening tax years which have already been signed off and agreed with HMRC; and that there is a lack of flexibility for those in financial difficulty who want to settle.

The Loan Charge goes against the **rule of law** in re-opening tax years that would otherwise be considered closed. Furthermore, the Loan Charge is punitive in that it combines loans received over many years and calculates as if they were income in a single year – meaning that most individuals will also pay tax at a higher rate.

There have also been concerns that HMRC have been slow or inaccurate in providing calculations to people wishing to settle, and that the tone of letters could be seen as aggressive. HMRC acknowledge that the service provided has sometimes fallen short and they have moved resources to deal with the large numbers of people who have shown an interest in settling.

HMRC's own statistics disprove this point. In January 2019 HMRC stated that 6,000 settlements had been agreed, in July 2019 that number has barely risen to 7,000. By HMRC's estimates there are 50,000 individuals that will be subject to the Loan Charge, so only 14% have reached a settlement agreement.

More generally, there have been concerns about whether HMRC's treatment of taxpayers who need additional support could be improved, and whether a proper overall balance between enforcement and fairness is being observed by HMRC.

The Loan Charge APPG has been informed of five suicides that have been linked to the Loan Charge and have referred themselves to the Independent Office for Police Conduct (IOPC) in at least one case. This is a very clear statement that HMRC's treatment of individuals has fallen well short of what would be expected.

There have been repeated calls for HMRC to set up a dedicated helpline for those struggling with the mental health impact of the Loan Charge. HMRC has so far failed to do that. The extent of HMRC's assistance to those vulnerable individuals has been to point them towards charities such as the Samaritans.

The Loan Charge Action Group set up its own helpline and its team of volunteers have received numerous pleas for help over the past 12 months. Without this volunteer helpline, these people would have simply had nowhere else to turn.

<u>New Measures</u>

In response, the Government has now agreed with HMRC some important changes:

1. HMRC will publish guidance to make specifically clear in relation to the Loan Charge that HMRC will not seek to tax the same income twice.

This guidance would be most welcome but this must also address those who have already settled and where HMRC have added Inheritance Tax (IHT) to the settlement. Paying income tax and IHT on the same loan is very clearly an example of being taxed twice.

2. HMRC will take a more collaborative approach to communications about the Loan Charge, drawing on advice from the Chartered Institute of

Taxation and the Institute of Chartered Accountants of England and Wales, among others.

Again, this is most welcome but it is somewhat too little too late without a suspension being immediately put in place to ensure that this advice can be taken in a proper and timely manner

3. HMRC will not apply the Loan Charge to a tax year where an enquiry was closed on the basis of fully disclosed information.

If an enquiry was opened and subsequently closed by HMRC then it is of course totally correct that no tax should be due. HMRC should not be allowed a second bite of the cherry.

This new measure introduces a new disingenuous meaning to the term "closed". Normally, where HMRC has failed to open an enquiry, after the statutory time limits those years would too be classed as closed. The Loan Charge should not apply to these closed years, as it is effectively a punishment for HMRC failing to open an enquiry.

Where HMRC have opened an enquiry those taxpayers already face the potential of receiving a large tax bill, but those individuals have the right to argue their case in court – a right that the Loan Charge removes.

4. HMRC will exercise additional flexibility for individuals settling under the published terms who are in genuine hardship. Where a person has no realistic prospect of paying tax due under the Loan Charge, HMRC will stop pursuit and leave any unpaid debt to be collected later only if their circumstances improve, in line with current practice.

Who defines genuine hardship? Receiving a tax bill of tens of thousands of pounds is likely to leave all but the wealthiest in hardship – the individuals caught up in this fiasco are ordinary hard-working people.

This is also not in line with HMRC's recent practice. HMRC have suggested that assets need to be sold, that loans should be taken out and have threatened to put charges on property and similar. We are aware of people being asked to pay twice their monthly income to HMRC, people approaching retirement being told to pay the same amount for numerous years without any consideration to the reduction in income and many other examples which simply do not tie in with the above suggestion.

HMRC will set out further detail on items 3. and 4. in the coming weeks.

Would it not then make sense for the minister to announce a suspension to the Loan Charge and settlement activity whilst these new measures are developed and published? It would be unfair on individuals who settle with HMRC in the meantime if he does not.

<u>Further support for MPs</u>

I am aware that the loan charge has been raised by many individual constituents and it is important that Members of Parliament have the information they need to understand and assist with any concerns.

HMRC are keen to take a still more proactive role in briefing and assisting colleagues who may have concerns about the loan charge. HMRC officials are also happy to discuss with them and any affected constituents their specific cases, subject to proper confidentiality.

If you have any questions about the Loan Charge, please do not hesitate to contact me.

The Loan Charge Action Group would also make this offer to all MPs as we have an in-depth knowledge and understanding of the Loan Charge and would happily arrange for members to meet with any MP who wishes to glean the truth and extensive facts regarding the Loan Charge.