

Treasury Sub-Committee

Oral evidence: The conduct of tax enquires and resolution of tax disputes, HC 733

Monday 10 December 2018

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Watch the meeting

Members present: John Mann (Chair); Mr Steve Baker; Mr Simon Clarke; Charlie Elphicke; Stewart Hosie; Wes Streeting.

Questions 91-120

Witnesses

I: Ray McCann, President of the Chartered Institute of Taxation, and Tony Lennon, Freelance and Research Officer, BECTU Sector, Prospect.

Written evidence from witnesses:

– [Chartered Institute of Taxation](#)

Examination of witnesses

Witnesses: Ray McCann and Tony Lennon.

Q91 **Chair:** Good afternoon and welcome to Parliament. There is nothing much going on today, so most phones are switched off. Nothing dramatic will happen during this session external to this room, I am pleased to say. You are welcome to stay in Parliament all day if you need a bit of entertainment. For the record, could you please introduce yourselves?

Tony Lennon: I am Tony Lennon, freelance and research officer for the BECTU sector of Prospect. My specialism is in dealing with freelance members working in film, television, theatre and events, many of whom are self-employed and some of whom work through personal service companies.

Ray McCann: I am Ray McCann, president of the Chartered Institute of Taxation.

Q92 **Chair:** Gentlemen, can I start by asking you about IR35 reform and loan charges? In your view, what are the concerns?

Tony Lennon: I think this is one for Ray, because the whole business of loans seems to happen on a sectoral basis. In our sector, film and television particularly, I have had two members out of about 15,000 ring and ask for advice on being caught in one of these loan arrangements. They are pretty unknown in our sector. I felt quite sorry for the ones I have spoken to because they had entered into this not knowing that it was questionable and had been put in a position where they faced very large bills. One of the people I spoke to said, "I'm probably going to have to declare myself personally insolvent to sort this one out." But, for workers in the film and TV sector, it is not an issue.

Ray McCann: The institute has expressed reservations over the loan charge plan from April, mainly because it is unprecedented legislation. It is being widely criticised as retrospective. From a personal viewpoint, I don't believe it is retrospective in the conventional sense, but it has a retrospective effect. In reality, the retrospective effect actually displaces all the protections that taxpayers are given by Parliament in terms of getting certainty for their affairs of the past. We have a situation where even an individual who has disclosed the loan arrangement to HMRC will still nevertheless be caught in April for quite an extensive period back—say, to 2006 and 2007—and will have a very substantial liability in relation to that.

We have made representations to Government and to HMRC. We are trying to find a situation where we can bring about something that will strike those who are caught by this legislation as a bit fairer, but, equally, we have to balance that. Again, from a personal perspective, a change like this was long overdue. These arrangements have just gone on and on and on. I have looked with some incredulity of late at some of the individuals



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who have used these arrangements right up until 2015-16. While they may be forgiven for having some sense, going back to 2010 and before, that these types of arrangements were sanctioned—if not sanctioned by HMRC, certainly HMRC did not appear to be too fussed by them—I don't think the same can be true in 2015-16.

There is a failure at all levels in terms of how HMRC have operated over the years. There is the delay in a change like this being brought forward by the Government, but also there is culpability on the part of those who have used these arrangements. Many of them, I suspect, have simply closed their eyes to the fact that they get a very advantageous tax and national insurance position and have been prepared to go along with representations sometimes made by promoters—in fact, quite often made by promoters who are outside the UK. In some of the stuff I have looked at, by and large they will say anything to sell that scheme. I have seen some really absurd claims being made with regard to the veracity of these arrangements.

Q93 Chair: What should the Government do about those promoters?

Ray McCann: As the law stood, there is no real sanction that the UK can apply against someone based, say, in the Isle of Man. Obviously, the UK could complain to an Isle of Man regulator, but it is uncertain in my mind as to whether or not the person acting in that way would necessarily breach any regulatory structure offshore. It is only in recent years that the UK has introduced rules that would allow the UK or HMRC to punish a promoter who was making outlandish claims and selling egregious tax schemes, irrespective of whether they were successful under the law or not.

Those rules have only appeared from 2015 onwards. HMRC's sanction against an offshore promoter is very limited. Against an onshore promoter, it is limited until you get to around 2015-16, by which time I would suspect that most of the UK promoters of this had moved out of that market because they saw the writing on the wall—if not well before that. I know, from talking to some who used to sell these schemes, going back in the distant past, that they had moved away from them once the disguised remuneration rules were announced in 2010.

Q94 Chair: When it comes to those who are offshore, what percentage of the market, on an ongoing basis, would they have? Is it the overwhelming majority?

Ray McCann: I'm not sure it would be fair to describe it as the overwhelming majority because I simply don't have the data to show that. I am convinced in my own mind that a very substantial proportion of these schemes were marketed and promoted from offshore. Certainly some of the more notorious providers of these schemes are based in the Isle of Man and have been based in the Channel Islands. Going back to my time at HMRC—I left HMRC in 2006—I had been heavily involved in targeting and trying to combat employee benefit trust avoidance for quite an



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extensive period prior to leaving. It was almost always offshore promoters who were behind it—certainly with the more egregious types of planning.

- Q95 **Chair:** Mr Lennon, are you suggesting that it is incredibly rare for your members to participate in any comparable scheme? If so, why? Why has it been unattractive to them?

Tony Lennon: I think it is incredibly rare. Out of 14,000 or 15,000 freelance members in film and television, we have been contacted by two. I suspect that if it were a widespread problem, there would have been a lot more phone calls. Why is that sector apparently free from that kind of arrangement? As I said, these things seem to go on a sectoral basis. A fashion will build up in a given sector where people start to think such things are fairly normal, but it has not happened in film and television. The other explanation is that most engagements in film and television are quite short. As I understand these arrangements, if you are trying to abuse the tax system, it makes much more sense to do it on a long-term basis.

Chair: Interesting. Wes?

- Q96 **Wes Streeting:** Mr McCann, some of the specific loan scheme examples we have seen, such as disguised remuneration loan schemes, seem to have become a major and widespread problem. Why do you think that those schemes are so widespread, and why is it so difficult for HMRC to get a handle on them? Lots of us have been struck by the fact that the enforcement is coming now, but these schemes have been running for the best part of a decade, including schemes that were given a number by HMRC and conducted under tax returns to HMRC. Why do you think it did not spot them and act sooner?

Ray McCann: I am sympathetic to that charge in so far as HMRC is concerned. I have seen examples, on request from some of the people who have contacted me, of copies of tax returns with DOTAS numbers on them. Because of my personal background and connection to DOTAS, I find it quite irritating that HMRC seems on a number of occasions—I don't know how many, but my hope and suspicion is that it is quite a small number relative to the total—not to have opened inquiries even when there has been a DOTAS number on the return. I feel a touch of personal embarrassment, in the sense that I put quite a lot of effort during 2004 and 2005 into emphasising that if you put a DOTAS number on your tax return, it was certain to get an HMRC inquiry. That is slightly personally disappointing.

To understand why they are so popular, you have to go back to the Lawson chancellery of the 1980s. Until then, national insurance—particularly employers' national insurance—was a bit of a Cinderella when it came to deductions. It was at quite a low rate, but during the 1980s it started to rise and rise. It has now got to the point where national insurance can be among the largest contributions that some big employers make to the Government. Equally, from an employee perspective, national insurance is quite a high proportion of what they pay in overall taxes. That



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has created a market full of people who have been readily willing to find ways whereby individuals can be rewarded in a way that does not engage either the national insurance legislation or the pay-as-you-earn regulations.

During the 1990s, there were a whole range of exotic schemes involving gold bullion, silver bullion, platinum sponge, reversionary interests in offshore trusts and all sorts of things. They were all designed not to attract employers' national insurance contributions in particular. The Revenue and the Government clamped down on them towards the end of the 1990s, and they started to give way to employee benefit trusts, which became very popular because they were seen as providing the same benefits.

Until 2004, when DOTAS started to come into the market, it was generally the Revenue's policy not to advertise the things that it did not like; it never made public pronouncements like, "We don't like this or that scheme—if you use it you will get investigated." Even today, it is a bit of a niche market finding information that makes clear the type of thing that the Revenue does not really like and is investigating, and even then it is quite limited by reference to the total.

Those schemes became incredibly popular simply because they offered huge advantages to those who were able to use them to pay less in national insurance contributions and less tax under the pay-as-you-earn regulations. That is the simple reason, but they are also popular because they do not require sophisticated arrangements; you just need an individual who is potentially liable to quite high levels of pay-as-you-earn or national insurance contributions, and it works. It is not like a scheme within the financial markets, where you need quite sophisticated facts and so on.

The Revenue at one time used an expression, "plug and play": anybody could use it, you just had to sign on the dotted line and pay whatever fee was there, and you were away. That is why they gained popularity, and they kept being popular because the fixes that were put in place were never really quite there. That was combined with an approach the market took: it found an incredible way of differentiating one scheme from another, even though for all intents and purposes the schemes were identical. I describe it as, "The change in law doesn't apply to our EBT because ours is on blue paper and yours is on yellow paper." Sometimes it gets as ridiculous as that.

- Q97 **Wes Streeting:** Turning to think about individuals' motivations for signing up, one of the things I have been struck by in the loan charge furore is that if you listen to HMRC, it couches it in quite straightforward terms: "There are people, fellow citizens, who are avoiding paying their fair share of tax by investing in a scheme that looks too good to be true, and if it looks too good to be true it usually is too good to be true. Therefore, there has to be enforcement." Most people, on principle, will think, "Well, I don't like the sound of that; that's absolutely right and HMRC has got them bang to rights."



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When we look at individual cases, the circumstances do not appear to be quite so straightforward. I am thinking about a couple of my constituency cases: a guy comes from overseas to the UK and takes professional tax advice, with IR35 lingering in the background. He is told to steer clear of some of the troubles around that, and this is sold to him as a scheme. He thinks, "Well, a 20% contribution sounds about right for someone who is self-employed, given that you do not get holiday, pension and all those sorts of things. So I know I am paying my tax and I know this is legitimate because I have had professional tax advice." Similarly, I have another constituency case of a mother who had previously had a limited company, took quite a period of time out of work to raise a young family and returned to work, with IR35 again hanging around in the background. She takes professional tax advice and thinks, "Well, rather than setting up a limited company again, this scheme sounds more appropriate, and 20% sounds about right, given that I'll be self-employed." Both those people now face potential costs of anywhere between £100,000 and £250,000. These are not very wealthy people who have anything like that money to spare, and I think most people, looking at those cases, would take a more sympathetic view. I certainly have.

I wonder what sense you have of the profile of people who have been caught up in this and their motivation, because this does not sound to me like celebrities buying helicopters and all sorts of other obviously elaborate schemes to avoid paying tax. It sounds to me like people who took advice, acted in good faith on advice and have never been given any contrary advice by the Revenue. Are my cases typical? Should we be sympathetic? Or do you think we should be taking a harder line, more consistent with HMRC's view?

Ray McCann: My preference with these things has always been that, if we change the law in the way the Government have done from April next year, we should have some sort of generous approach whereby we give credit to people that is intended to get them out of these arrangements before the law changes. It is important to recognise that the loan charge is a general application to most employee benefit trust-type situations, so it would apply to the biggest international bank, and some of the banks in the City used employee benefit trust arrangements to reward their employees and senior people by way of bonuses. Hundreds of millions of pounds were involved. The Revenue has had various arrangements over the years to try to allow people to clear up their tax position, but for various reasons those arrangements have never really worked for this group, which is mainly contractors. I think it is because they come in to this very late in the cycle, so by the time the contractor loan arrangements are being cleared up, the banks and so on and all the big companies have largely settled, either because they have lost in the courts—for example the Dextra group, which lost in 2005—or they have been able to take advantage of the employee benefit trust settlement opportunity.

It is quite difficult, certainly for me, to look at most of the individuals I come across and feel sympathy for them, in the sense that I do not understand how they could get into this type of arrangement and not think



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that there was something untoward about it. I am sympathetic towards someone who has disclosed this on their tax return and was not taken up for inquiry; I do not think HMRC should easily dismiss that that person has tried.

Likewise, it has been put to me that a number of people were put into a situation where it was this arrangement or no job. I have never met anyone who was actually in that situation. I do not know the extent to which it is a myth. However, if someone is happy to show me some information to make clear that that is the case, by all means I would accept that it had probably happened.

There are so many people involved that I would not lightly dismiss the possibility that there is some category of individuals who fall into that type of scenario, but I think that the majority of people in these loan schemes knew exactly what they were trying to get out of it. I have seen some numbers that are really difficult to look at without wondering how someone could possibly have believed that that was an appropriate way to manage their affairs. How could they possibly think that earning £7,000 a year and getting £150,000 in a loan could possibly be an appropriate way to run their affairs year after year?

It is quite a challenge for someone who has any knowledge and experience of these arrangements to look at this with great sympathy. However, I am sympathetic to the situation that a lot of people end up in. That should be resolved with more generous terms whereby they can get out of those arrangements. It sticks in the craw for some people that someone who has done a tax avoidance scheme gets a generous offer to settle it, but that is the way it has been for the last 10 years.

Tony Lennon: May I join in? I hesitate to do so because I have already said that these loan arrangements do not really feature in our bit of the economy. However, to make a general point, in sympathy with your constituents, I am often surprised by the lack of knowledge that many of our members have about the taxation system, especially if they are not in an employment relationship and are in one of these atypical arrangements.

I completely agree that, in life, you should always apply the “too good to be true” rule, but there are people out there in these arrangements who have taken professional advice—perhaps from members of Ray’s organisation—and who believe that they are doing the right thing. I have to say that my experience of our members is that they generally want to pay their tax properly, partly because it enables them to sleep at night but partly because they know that they are doing the right thing. Prospect’s position, like all unions, is that our members, and citizens, should pay tax according to the law. There is absolutely no question about that.

Ray McCann: If I can add to that, it is undeniably the case that some members of the Chartered Institute of Taxation have at points in the past been involved in giving advice to clients in this area. As the Committee will



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know, we changed our rules in 2015 to require our members to have more regard to what the tax system is intended to achieve for the country as a whole. The intention of Parliament, even though people dispute how to identify that in the legislation, is nevertheless real. It is not the place of the institute or its members to undermine what parliamentarians intend to achieve with the changes that they make to the tax system.

I can say today that, if I came across one of my members advising on loan-type arrangements and pretending that, somehow or other, they were fine and not objected to by HMRC, and if they did not give their clients due warning that they were likely to be involved in a long-running dispute, I would have no problem referring them to the independent Taxation Disciplinary Board, which has the power, in the extreme, to strike a member off. However, I take the point: the claims made by the main promoters of these arrangements were outlandish at best.

Q98 Mr Clarke: Mr McCann, thank you very much for coming in today. I want to discuss retrospective legislation, which obviously plays a massive role in adjudicating the fairness, or otherwise, of what the Treasury has been doing. Many are concerned that the disguised remuneration loan charge is retrospective legislation, although obviously the Treasury and Revenue and Customs deny that. What is your view?

Ray McCann: I do not think it is retrospective legislation as we understand it. For example, let us say that these types of loan arrangements appeared first in 2011. The legislation does not make it taxable in 2011—that would be retrospective legislation—but it undoubtedly has a retrospective effect, because it will tax the loan made in 2011, regardless of the fact that it does not go back that far.

As I said at the start, I have described it as worse than retrospective legislation, because it displaces all the protections that Parliament has put in place. Those protections will or won't be available to the taxpayer, depending on the behaviour, but it would be rare to see very many of the individuals involved in this as capable of being accused by HMRC of having deliberately evaded tax, which gives the Revenue the longest period—the 20 years. The loan charge has been drafted in such a way that it applies from 1999, but it would be incredibly surprised to find anyone in a loan-type arrangement as far back as that. I suspect that the majority are from 2005-6 onwards.

It is not retrospective, but it does have a retroactive impact. Equally, if it was retrospective, it would change the law from 2011. To use my example, the tax would be due and the national insurance would be due, and there would be interest on it, so it would multiply the cost to the individual quite significantly, whereas next year it is calculated on the basis of the tax as though it is actually due in April '19. That in itself is not good, because you could have a relatively low-income individual who is suddenly paying the highest rate of tax because there is this clogging effect, in terms of how you calculate the loan. As I said at the start, the way this legislation has been enacted is not something we should easily allow to go without some criticism, because of what it does in relation to



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the laws of the country around how far back HMRC can go to collect tax from an individual, based on that person's behaviour.

- Q99 **Mr Clarke:** If it were found or conceded to be retrospective legislation, what difference would that make to the validity or enforceability of the charge?

Ray McCann: If it was actually retrospective legislation—let's assume that it is retrospective legislation that is still effective from April next year—the extent to which HMRC could apply it to an individual would be determined by reference to the law as it stands, in terms of how far back HMRC could go. If you go back to my earlier example of an individual who has disclosed the loan arrangements and included a DOTAS reference on their tax return, it seems to me that, without some further change in the law, that person would be beyond the reach of HMRC, in terms of applying the loan charge. In theory, it would still apply for the year, but that person would be protected by the normal estoppel that is on the Revenue under the Taxes Management Act 1970. If the Revenue had cause to believe that the person had deliberately evaded tax—as I say, in this context, that is probably unlikely—they would have a longer period of time. In most cases, it would be well beyond the point at which the Revenue could try to collect the tax.

- Q100 **Mr Clarke:** As a matter of taking this to a higher level of theory, what is the tax profession's view of retrospective legislation in the round? The Treasury would arguably defend it as a necessary recourse to prevent tax avoidance, but could it also be construed as an abuse of the rule of law?

Ray McCann: It is fair to say that the Government do not introduce retrospective legislation particularly frequently. The last significant retrospective legislation was in relation to stamp duty land tax schemes, when two separate retrospective legislative amendments were made. They were fortunate, in the sense that the retrospection was not particularly long—I think it only went back two or three years, or something like that.

We have objected to this for the reasons outlined: it is not strictly retrospective, so it is side-stepping the protections. As a general principle, we are not in favour of retrospective legislation because of the impact on taxpayer certainty. Nevertheless, we can't object absolutely, because Parliament has to be able, from time to time, to look at something and decide that it is so egregious that retrospection is required in the anti-avoidance area. It should be quite a high bar, and Parliament shouldn't pass retrospective legislation willy-nilly—of course, it generally doesn't. It should be clear why, for example, this particular group of individuals should be subject to the rule enacted in the way it has been, but, overall, retrospective legislation is something we should try to avoid.

- Q101 **Mr Clarke:** Mr Lennon, do you have any comments on the issue about the desirability or otherwise—

Tony Lennon: Of retrospective legislation?

Mr Clarke: Yes.



Tony Lennon: As a general principle, ordinary working people need to know where the goalposts are, and it is a bit unfair to say, "The goalposts have moved, but not from today; they moved sometime back in history."

Q102 **Mr Clarke:** Mr McCann, you obviously speak on behalf of the Chartered Institute, and therefore you are well placed to opine on the profession's evaluation of the landscape. Would someone well versed in tax law anticipate that the Government might respond to tax avoidance with retrospective taxation, given that there is a history of this? I point to the example of the Finance Act 2008, which addressed earlier schemes used by some contractors. In other words, was it a foreseeable risk?

Ray McCann: In my time at HMRC, one of the things that I was responsible for, and partly involved in, was the drafting of the statement made by the then Paymaster General in December 2004, which warned of the possibility that the Government would introduce retrospective legislation, particularly in the employment area if there were continuing attempts by promoters to sell schemes in the market that essentially abused the pay as you earn system or the national insurance contribution system.

The difficulty is that that is quite easily said. Coming back to an expert view, you know it is there, you know what was said, and you were involved in the drafting of it, but that does not mean that the average person who is attracted to these schemes will necessarily be aware of that. Certainly I have not seen anyone selling these schemes drawing anyone's attention to it.

We can have this ideal model where we think, "Well, the Government has warned of retrospection, and it has done that in various avoidance areas. It has warned that various things would be subject to retrospection. Sometimes it has acted on them; sometimes it has not." The difficulty is in being safe or confident that the general public are aware of those pronouncements and those potential changes before they get involved in this type of stuff.

One thing that I hope will come out of this is greater public awareness. If HMRC is saying that some things are too good to be true, that is perhaps a good warning that people should adhere to before they get involved in a scheme.

Mr Clarke: Caveat emptor. Thank you very much.

Q103 **Chair:** Mr McCann, is the contractor loan settlement opportunity working well?

Ray McCann: I have been critical of it. I do not think it is working particularly well. Coming back to the point I made earlier, I think it should be more generous. I do not think it is right that HMRC gives people credit against the loan charge only in circumstances where they are prepared to voluntarily pay any tax and duties that are due for years that are out of time.



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Typically, the way the scheme will work is that if you pay, let's say for argument's sake, a liability from 2008 voluntarily, they will not charge you interest on it and they will give you credit against the equivalent loan charge for that year. However, my preference would be that out-of-time years are left out of account completely.

There are two reasons for that. First of all, I think that is a fairer way of approaching long-term situations like this. Secondly, that is the way the earlier employee benefit trust settlement opportunity operated. Where the Revenue were satisfied that you had at least made an attempt to notify them, HMRC would leave that out of account for the disguised remuneration part 7A rules themselves.

I do not understand, and I do not see any reason, why it cannot be consistent with that rule. On its own, that would deal with those individuals who claim to have notified HMRC at the appropriate time that they had a loan arrangement. As I say, looking at the tax returns of some of the individuals—only a small number, inevitably—I can see on those tax returns sufficient information that I think most HMRC inspectors looking at that would have thought, "Yes, there's something going on here. I need to make an inquiry."

The settlement opportunity gave credit for those years that were out of time for whatever reason, particularly where the taxpayer had made an attempt to notify HMRC. That would take away a lot of the unfairness regarding how the settlement opportunity works. Ultimately, it is not right that HMRC should insist on voluntary payment for out-of-time years simply to get a credit against the forthcoming loan charge.

Q104 Charlie Elphicke: With these matters, is it not the case that the law on the question is quite clear whether taxpayers knew it or not?

Ray McCann: Do you mean on the loan charge itself?

Charlie Elphicke: Yes.

Ray McCann: Yes, I think the law on the loan charge is clear. As I said earlier, left to me I would have introduced a similar charge many years ago, because it was one of those areas where it just went on and on. Whether the legislation is capable of being properly understood by a layperson, which is effectively what we are talking about—an IT contractor, or whoever is involved—is a slightly different question. However, in terms of what the legislation is intended to achieve, I think it is clear.

Q105 Charlie Elphicke: There is a difficulty, isn't there? If I buy a stolen car, the loss of it then having to be returned to its owner sits with me, does it not, unless I am able to recover it from the person who sold it to me? Is the issue not whether they should be paying the tax or not, but the person who sold them the dodgy product?

Ray McCann: Let's accept that that analogy is correct. The situation we have here is that the loan charge is, first and foremost, directed at the



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employer. Where we are going to have a problem is that large numbers of the individuals were involved in effectively fictitious employers. Certainly for some of the ones that I have seen, I do not believe there was any substance in the employers at all. It was mainly a name in order to provide a cash-flow arrangement.

If you go back to the infamous Jimmy Carr, the K2 scheme is a loan scheme. That was 2012. Coming back to the point I made about how a layperson cannot easily be expected to see all the nuanced pronouncements that HMRC or the Government might put out, it would be difficult to suggest that anybody could have missed Jimmy Carr being all over the press and all over the television around his loan scheme. At the time, I did not believe for a minute that the K2 arrangement involved a real employer requiring a real employee to do real things. It was a cash-flow arrangement, which is, I am sure, why Mr Carr gave it up fairly quickly once it was pointed out to him that it was a tax-avoidance scheme.

The difficulty is that if you are going after the employer, you have to find that employer. I am sure there are a number of probably UK-based employers who are in the firing line from HMRC, but my suspicion is that it will be the minority of users. The numbers involved range from 50,000 to 100,000, so there is bound to be someone who HMRC could catch, but it then defaults down to the user to pay the tax. I suspect that, in many cases, it will quickly default to the user so they will all be in line for quite substantial tax bills—even where they have had relatively modest amounts of loan.

Q106 Charlie Elphicke: If I am the taxpayer and I have had one of these schemes, and I have been told that if I am paid in this kind of way, I miraculously will not have to pay any tax at all, do I not have some responsibility to think that, if it seems too good to be true, it probably is?

Ray McCann: I do not disagree for a second. I have to temper my irritation with these arrangements. I have looked at several of these arrangements at various times and I have seen numerous types of employee benefit trust arrangements. They all involve a large proportion of, "Nod nod, wink wink. You will get this money."

We can say what we like about the tax, but the simple fact is that the majority of people involved in the arrangements cannot afford to pay the loan back. If they cannot afford to pay the loan back, that goes to the very heart of what they thought they were taking on in the first place. The arrangements were sold—I am pretty certain that the Revenue will never find a piece of paper from a promoter saying, "Under no circumstances will you ever have to pay this loan back," but I am equally certain that most if not all of the people involved knew that they did not have to pay it back.

If I had my choice, everyone who is caught by this would pay the tax, but that is not where we are. We have to face up to the reality of the fact that not everyone, but probably a large number of them, will find it impossible to pay back the tax that is due, or would certainly find it impossible to pay it back within a reasonably short period of time, because some of them



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have taken on very significant “debts”. I have seen some with hundreds of thousands of pounds-worth of debt.

Q107 Charlie Elphicke: The issue I have is that my constituents in Dover and Deal, who pay their taxes—who do not have any choice in paying their taxes, because it is automatically operated by PAYE—will say, “How can this be fair? Why should I pay more tax to make up for the fact that this person tried to game the system and it didn’t work out for them? That’s not fair on me.”

Ray McCann: Absolutely. The extent to which you look at this as fair depends on your perspective. If you are caught by the loan charge, you are inevitably going to think that it is unfair. If you are a pensioner who has paid his or her tax their entire life, perhaps—worse—waiting for an operation on the NHS, listening to the news and being told that there is a lack of resources, why would you have sympathy for someone who has received sometimes hundreds of thousands of pounds over the years and not paid tax on it? You are never going to be sympathetic in that situation, so you are absolutely right to have that level of concern.

The difficulty for me is coming from how we practically get these things cleared up. Whatever else we might think, I do not see HMRC being able to tackle 100,000 individuals and bring them all to book in a nice orderly fashion whereby they get their chequebooks out and pay their tax. Therefore, we need extraordinary measures to try to get them out of the situation, otherwise we further clog up HMRC’s resources more and more.

Q108 Charlie Elphicke: HMRC has care and management powers. Looking at those powers, do they actually have discretion, or is this a case where it is so clear that it would be ultra vires for them to try to exercise discretion because they have a duty to collect the tax and there is no doubt?

Ray McCann: My personal viewpoint is that HMRC does have discretion to enter into a settlement arrangement with these individuals. I do not think it has discretion—let us just say the members of the Committee are all loan charge—to discriminate for no particular reason against any of the individuals; it has to provide some consistent basis whereby it settles it. I am of the view that HMRC could compromise on its claim against any particular individual, tailored in a way to allow that person to clear up their tax affairs without having then to go for bankruptcy. Some in HMRC will deny that; an HMRC lawyer would probably throw his or her hat in the air and shout rage at that suggestion.

From the discussion I have had with HMRC I think that they are keen to try to engage with as many of those people as possible and get them cleared up or on the road to being cleared up before the loan charge comes in. I think they will have less discretion once the loan charge is effective law from April next year, because any settlement they reach would clearly go against what the legislation provides for that person to pay. There is a window in which HMRC can provide better settlement arrangements, but that window is rapidly closing.



Q109 Charlie Elphicke: So far, do you think HMRC takes too rigid a view of how disguised remuneration cases should be settled?

Ray McCann: The difficulty with tax avoidance issues is that an awful lot of emotion gets brought into it. Perhaps I was like that when I was in HMRC: you see an egregious scheme and you start spitting feathers—you are determined to try to bring the taxpayer to rights. You can sometimes lose objectivity of what you are trying to do. Tony here knows about IR35. I have yet to see an IR35 inquiry run by HMRC that was not full of emotion and lot of bad spirit. We have to take that away and try to be more objective.

If you take a loan charge user who is confronted with a liability of £250,000 to £300,000 and they simply cannot pay, is it really in anyone's interests to force that person into bankruptcy? In that case, the revenue probably gets nothing in any event. I am satisfied from the discussions I have had with some of the more senior people in HMRC, who are involved in trying to resolve the loan charge, that they are minded to the idea that they want to try to help people involved in it to get their position cleared up. Obviously, there will need to be openness on both sides in terms of properly revealing assets and borrowing capacity, but until the individuals affected contact HMRC and try to see what type of settlement arrangement is on offer, they will never know. I have been encouraging them of late to contact HMRC. If they get in touch with HMRC and it says, "No deal; you have to pay the whole lot," that is one thing—at least they have an answer—but this strengthens the case for those claiming that it is unfair.

Q110 Charlie Elphicke: HMRC has a large stack of open inquiries. What is the best way that they should deal with them to get rid of them all?

Ray McCann: Over the last 10 years or so they have had various facilities, clearance opportunities and so on. Three years ago I called for one final attempt—just a general clearance opportunity that was fairly generous, to try to encourage people in, get them signed up to some sort of settlement arrangement that allowed them to put the past behind them but also commit to try to ensure they did not get back involved in such schemes. They already had their litigation strategy, which in very broad terms says if they think they will win, they cannot give in. We have created an atmosphere whereby the only part of business life in the UK where compromise is not allowed is in relation to tax.

It seems to me that if the tax system deviates from what would happen in normal commercial practice, we end up in a position where I am reasonably confident that, if I owed the revenue £100,000 and the most I could offer was £90,000, that offer of £90,000 might not be treated with open arms. I would be as likely to see HMRC say "No, no. We want £100,000." There is too much rigidity in how HMRC tries to bring these things to a close. That is an area that we could look at. I have written several times on the loss of discretion that HMRC it has suffered since 2001 with the Wilkinson case. I think they have sufficient discretion, and



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that is key to try to bring all the long-running cases to a close on terms that even the loan charge people might regard as fair and reasonable.

Q111 Mr Baker: I would like to pick up on an issue about retrospective effect. Mr Lennon, you gave a very good description of the goalposts moving and people being told that they had moved a while ago. Mr McCann, you drew a particular distinction—I think it was this but do not have the transcript—between retrospective effect and normal retrospective action. Could you flesh out a bit the distinction that you draw?

Ray McCann: If I may, I will go back to the example I gave. Let's say I did some scheme in 2011—I didn't, but let's say I did—and I saved £50,000 in tax. By 2018 the Chancellor has got really fed up with this scheme and he decides that he doesn't like it and is going to change the law retrospectively, so the scheme I used in 2011 does not work. In theory I owe £50,000, but there is a whole body of legislation in the Taxes Management Act that will protect me from having to pay that tax, depending on what I have done. The general time limit rule is four years, so after four years, if the Revenue has not caught up with me, I am off the hook. If I have been careless in my affairs, that time limit is extended to six years, but if I have deliberately set out to evade tax, the time limit is 20 years.

Let's suppose instead that, as we have here, we have a retrospective effect: the Chancellor decides, "Well, from April next year, I'm going to bring that £50,000 that you saved back into tax." All those protections that I have referred to disappear. The only saving I get is that the tax is treated as arising next year, rather than in 2011, so I won't have a late payment interest charge on it.

Proper retrospection means that some taxpayers will not have to pay at all. Those taxpayers who are actually under inquiry with HMRC would still be caught, regardless of how far back the retrospection went, so if it was retrospective back to—

Q112 Mr Baker: I see. When you first used the term "retrospective effect", I thought you were suggesting that it was less draconian, but it feels to me, now you have explained it in more detail, that retrospective effect is actually more draconian in relation to the rule of law and taxpayer certainty. Have I understood you correctly?

Ray McCann: Again, it is more complex than that, because you have to factor in how the interest position works. Pure retrospection would have collected my £50,000, plus late payment interest because I had not paid at the time, so, from 2011, I might have to pay, say, £70,000 when you add in interest. The retrospective effect would collect the £50,000, but not the interest, so I would end up paying £50,000. So it has pluses and minuses, but the real plus, to someone faced with retrospective legislation, is that they may never have to pay at all, depending on how far back their particular scheme went.

There was a controversial change some years ago to Isle of Man partnerships, which the Government concluded were abusive as well, and



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the retrospection was put in without limit of time. That was challenged through the courts and the people lost. And that went really far back, so they ended up with tax liabilities for those much earlier years, with interest on top and the potential for penalties, depending on the circumstances. So that's the key difference.

Q113 Mr Baker: Thank you. Mr Lennon, you explained that loans have affected only two, I think you said, of your members, but do you think that off-payroll working reforms have had any inadvertent or unintended effects on your members more generally?

Tony Lennon: Yes—are we moving to IR35 now?

Mr Baker: Yes please.

Tony Lennon: Yes. We have seen the change in the public sector in terms of the intermediary rules and where the liability for any unpaid employment tax rests. In our case, we have had a lot of experience of film and TV workers working for the BBC, which is the main public sector body that we deal with, but through Prospect, I have also seen instances of school inspectors, for example. I have seen instances of consultants in energy supply, the nuclear industry and areas like that who were working through personal service companies and whose situation has been reviewed as a result of the changes in the public sector intermediary rules.

I have to say that the level of compliance seemed to be fairly good. In other words, public sector engagers, partly because they have big HR departments, legal advice and stuff like that, were generally playing by the rules and not putting people in a position where, if they billed through a limited company, they were running the IR35 tax risk.

What we have seen happen inadvertently is this. A number of people who we believe are genuinely operating businesses in their own right—there is no deemed employment payment arising—and should be treated as self-employed, working through a personal service company, have been put on to PAYE. It's not a massive number, but a few have. There has also been a knock-on to another sector of the workforce, which is people who are working as self-employed sole traders. Schedule D is the commonly used phrase—it doesn't apply any more, but you know what I'm talking about. They have also been reviewed by public sector engagers, because they remembered that they have always carried the tax risk for PAYE that was not deducted from those people. In April last year, the IR35 changes introduced a new risk. So we have seen in that community a number of people, again, who we think are genuinely self-employed jobbing freelancers and who have been put on to pay-as-you-earn.

One of the problems has been that most public sector engagers seem to have latched on to the online employment status checker—CEST—which has some flaws in it. From our point of view, there are two crucial flaws. The first is that when it tests on provision of personal services it does not give enough weight to your right to send a substitute on a qualified basis; it is looking for an absolute right to send a substitute. The other flaw in



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that online checker is that it does not test at all for whether you have multiple engagers. Working for lots of different people of course is one of many indicators of potentially self-employed status.

Public sector engagers have tended to rely, I would say rather slavishly, on the online checker. They go with the result even if instinctively they think it might be wrong. Where they get an indeterminate output—there are cases where it will not tell you whether you have an employee or not—public sector engagers have tended to play safe by automatically putting you on the payroll rather than using their knowledge and experience to make a judgment about employment status.

Yes, there have been inadvertent effects. I repeat what I said earlier: people have to work within the law, but the law does acknowledge that you can work through a limited company, and in many circumstances you are not actually giving rise to a deemed employment payment because you would not be in an employment relationship if the dealings with the engager were different.

Q114 Mr Baker: One of the two flaws you mention is this issue of insufficient weight being given to people having multiple clients. What proportion of your members do you think have multiple clients?

Tony Lennon: All of them. Practically all of them.

Q115 Mr Baker: To what extent? Two or three, or tens? I just wonder what the distribution is.

Tony Lennon: Typical engagements in our sector are actually quite short. You could work one week for somebody, you could work another week for somebody else and you could work the following Tuesday for a third person. It goes on and on and on. There is a test case in this area—Hall v. Lorimer. Mr Lorimer was a member of our union, and I think he was able to demonstrate that he had had over 100 engagers in the course of a year. I would say that predominantly, our self-employed members, who are working mostly as sole traders, some of them through personal service companies, have a multitude of different engagers over the course of a given year.

Q116 Mr Baker: Mr McCann, looking more broadly at all people who are subject to IR35, what do you think is the population? Do you have any concrete evidence of what the population distribution is? The reason I ask is that my experience in IT was that people very often just worked for the one company. I am wondering to what extent people actually have multiple clients.

Ray McCann: I don't generally get involved too much in the IR35 space, although I have had some clients involved in IR35 inquiries. I have rarely seen anyone who does not have a number of clients. What I have typically seen among users of an IR35-type situation is a preponderance of income coming from a single client, with some other small ones. I think that is problematic for HMRC.



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I agree with the point Tony made about multiple clients. I would actually say it more strongly than Tony did: if, as in the *Hall v. Lorimer* situation, you have 100 clients in a year, it is almost certain that any judge would find that you were self-employed. To me it is inconceivable that you would hold 100 employments and be active in relation to each of those. However, of late, HMRC have been suggesting to me that each individual contract has to be tested separately. I think that is going too far.

With the IR35-type scenario, at the extremes you see cases that seem obviously open to challenge by HMRC, but you see other cases where it is difficult to understand why HMRC are challenging them at all, because there do appear to be multiple clients. But there are undoubtedly a number—I cannot give you even a percentage—where it is single user, effectively. That, essentially, is the classic model that IR35 was introduced to try to combat.

Q117 Mr Baker: Could I ask both of you why you think people choose to form companies rather than just being self-employed?

Tony Lennon: Often they don't choose. I can think of three or four routes in the film and TV sector that lead people into personal service companies. One is that they bump into an engager who has a policy of dealing only with personal service companies. It is not the choice of the individual. They are told, "If you want to come and do this engagement, you'll have to bill me through a limited company." Whether that engager has done a proper assessment of the employment relationship is not always certain. They may have done some generic assessment some time ago about how they engage people, but they tend to have a policy of, "You've got to bill me through a personal service company." It may well be that they are trying to avoid any risk of employment rights building up, or 13.8% employer's national insurance, but that is how it is. If you want to work in the industry, you will find that that sort of offer is made to you.

You will get other engagers who actually assess each case. At some point, they might say to you, "Well, we've looked at your employment relationship. It's a bit ambiguous, but if you bill us through a limited company, we will pay you gross and we won't actually put you on to the payroll."

The third route in is that it becomes fashionable. I suspect that that is why we haven't had loan agreements—because they haven't become fashionable in our sector, although they have become fashionable in other places. Individuals will get the herd feel: "Everyone else who does what I do seems to have a limited company so I ought to have one as well."

Lastly, people form companies because in some cases their business model means that's the right thing to do. But in my experience, although the formation of limited companies in many circumstances is viewed as being tax avoidance, the first time a lot of people in our sector ever find out that on share dividends they would pay lower tax than through income tax is when they go to meet the accountant, having decided for various reasons that they should set up a company.



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So the tax avoidance thing is not a major driver. The avoidance of NICs on the part of engagers is a partial driver, and I think ignorance, herd instinct and mythology is another driver—if everyone else is doing it, you feel that you really ought to do it as well.

We do not have a high proportion of personal service companies in our sector. We advise people that it is actually a lot easier, if you are genuinely self-employed, to work as a sole trader because it is administratively simpler; the dangers of not complying with the various filings that you have to do with Companies House, your corporation tax and things like that are completely eliminated; and it is a very straightforward way of doing things. I emphasise: self-employed sole traders pay the same income tax as everyone else.

The big driver of self-employment, or of choosing self-employment if you can in our sector, is that you can recover your business costs. One of the inadvertent effects of the IR35 changes in the public sector is that we are now seeing people, who we believe are genuinely running businesses in their own right, being put on to the payroll and for tax purposes treated as employees, but where they incur costs to provide their services—staying in hotels because they have an engagement 100 miles away from where they live—they are having to bear that from within their taxed income, their employee's income. It is not possible for them, because they are employees, to seek tax relief on those expenses, because even if they are just there for a day it becomes their normal place of work if they are an employee.

Ray McCann: Those who use a limited company for tax and national insurance reasons are attracted to it by the fact that until fairly recently there was a huge differential between the tax on dividends and the tax on earnings, to such an extent that until the rules were changed if you had a husband and wife running a limited company, they could have approximately £100,000 a year between them and pay no tax or national insurance, because they could take the majority of the profits out of the company by way of dividends. If you have a situation where the corporate tax rate is coming down, which it has been in recent years, to quite a low level, the only tax they end up being charged is the corporate tax at 19%, 17% or whatever it ends up as.

That has been hugely attractive and is the sort of area that has attracted the Revenue to look at those arrangements whereby the limited companies seem set up purely to take advantage of that, but it is not—or wasn't—limited to dividend taxation; you also got a hugely advantageous position in relation to capital gains tax if you ran the kind of company that had a client list, for example. You could sell that client list if you were retiring, get rid of the company and pay a 10% capital gains tax rate.

Q118 **Mr Baker:** Forgive me, but you have told two quite different stories there: people not even knowing that there are tax advantages in some circumstances; and people being very much motivated by that in other circumstances. To what do you attribute that difference in story? Is it who you represent—as simple as that?



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Tony Lennon: I would say it's partly the scale of people's earnings, because the celebrated cases under IR35 that involve tax bills of hundreds of thousands of pounds are, by definition, high-paid people who often engage an accountant. An accountant might well explain to you exactly the tax benefits of forming a personal service company. Most people who work in the film and TV sector, and actually in other areas of Prospect, will never run up tax bills of hundreds of thousands of pounds, because they don't get paid all that much to begin with. They certainly would never go near an accountant until they had to. I would argue that in the film, TV and entertainment sector generally, most people do not form companies for the primary motive of achieving a tax benefit. They do not do it for that reason. Inevitably they will find out at some point, because we always advise them "If you've got a company go and get an accountant; don't try and run it yourself". The accountant will explain the tax-efficient method of extracting money from the company.

Don't forget, in some circumstances it is perfectly legal. If there is no employment relationship there, it is perfectly legal. IR35 is designed to catch cases, quite rightly, where there is an employment relationship and PAYE and national insurance should have been deducted.

I go back to this sectoral theme that it is not a massively well paid sector. Some people do quite well. You will have seen various on-screen presenters being taken to tax tribunals and you will have read the outcome of the cases. Some of them are quite highly paid, I have to say, but they are outliers in terms of wage income, and they are the sort of people who would have accountants. Most of our members, if they are just jobbing freelancers, don't.

Ray McCann: And just to be clear, Mr Baker, I didn't intend that there would be the gap between Tony and me that you detected. My point is that quite often if you are setting a company up it can be, as Tony portrays it, happy coincidence that you discover that you get tax and national insurance advantages—or potentially, if you take them. Lots of people run limited companies and take relatively modest dividends. My point was that, where you are looking at a limited company structure purely for tax reasons, it is those types of advantages that are attracting you in—less tax, less national insurance contributions, and advantageous capital gains tax rates.

Q119 **Chair:** Thank you for coming. If there is anything that occurs to you that you think would be useful to the Committee, on reflection, either generic points or very precise detail, we would be keen to get some in, subsequent to this. I thought it was a very interesting session—very helpful to us in terms of mulling over these issues and some of the dilemmas, and if there are specific things you think ought to be happening, that you want to home in on, please communicate in writing to us, because we are very much open to that. Thank you very much for what was a very interesting session.



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Ray McCann: Just to make one last point, I think we have to find, between us, a way of encouraging those affected by the loan charge to talk to HMRC. That seems to be the biggest priority at the moment.

Q120 **Chair:** Well, you have mentioned a window of opportunity. If you have suggestions on what we could recommend then please pile them into us.

Tony Lennon: A last word from me, if I may: the entertainment sector has a long history of self-employment in one form or another. As far as we are concerned, it is legitimate self-employment and the nature of the engagements and the way people work strongly indicate self-employment. I would just like to express my concern that, in dealing with the abuses that are happening in areas like the gig economy—and I think it is quite correct that Government addresses those abuses—there is a danger that we come up with a one-size-fits-all solution to taxation of workers, which starts to undermine the self-employed status of members of my union and many other legitimately self-employed workers throughout the country. To leave you with my last thought about self-employment, the principal benefit for workers of self-employment is that they can recover their business costs. A self-employed sole trader, for example, pays the same income tax as anybody else does. It is all about business costs; it is not about avoiding employment tax.

Chair: I met a couple of your members in the early hours of this morning, who had travelled quite a distance.

Tony Lennon: I think you might be seeing some of them later as well.

Chair: Who knows who will be meeting them? Thank you for coming this afternoon.