

LOAN CHARGE ALL PARTY PARLIAMENTARY GROUP (APPG) - WRITTEN EVIDENCE (DFE0029)

Draft Finance Bill 2020-2021 inquiry

Introduction

The All-Party Parliamentary Loan Charge Group (Loan Charge APPG)

1. The All-Party Parliamentary Loan Charge Group (Loan Charge APPG) is an All-Party Parliamentary Group comprising of 237 Parliamentarians of all parties from both Houses of Parliament. Members of the APPG have concerns about the nature and impact of the '2019 Loan Charge' and they also have concerns about the wider context of fairness of tax legislation and about HMRC's conduct in enforcing it. The APPG's website is <http://www.loanchargeappg.co.uk/>.
2. The Loan Charge APPG welcomes and has been calling for effective action to stop the ongoing mis-selling and operation of unacceptable tax avoidance schemes and for action to be taken against those who recommended, promoted and operated the schemes now subject to the Loan Charge. The reality is that until now, HMRC and the Government have largely failed with regard to each of these.
3. The Loan Charge APPG is clear that people should pay the right amount of tax and, as laid down in the introduction to our Loan Charge Inquiry report, published in April 2019:

“...we believe the Government should clamp down on tax evasion and properly resource HMRC to do this. We also believe that the Government should prospectively close any loopholes that allow for unacceptable avoidance”.¹
4. The issue is that this has not happened – so we welcome attempts to do so and urge that they are meaningful and effective, to avoid another scandal like the Loan Charge Scandal, which has caused so much distress to those who used the schemes, whilst those who operated them have not been asked to pay any of the disputed tax and have faced no effective action for doing so.

Measures proposed by the Government/HMRC

5. We support the principle of taking action to close down schemes and pursue those behind the schemes, and indeed have been consistently calling for the

¹ Loan Charge Inquiry Report, April 2019, page 6 <http://www.loanchargeappg.co.uk/wp-content/uploads/2019/05/Loan-Charge-Inquiry-Report-April-2019-FINAL.pdf>

Government and HMRC to take decisive action to stop the promotion of loan schemes and pursue those involved. However, we are concerned that so far all the Government has announced are principles and little in the way of actual legislative change to tackle this problem.

6. The policy paper states, “the government has announced at Spring Budget 2020 a significant package of measures to tighten the rules that apply to promoters” and yet in reality there appears not yet to be more than broad themes.

7. We wish to see clear and detailed proposals, to properly stop the ongoing promotion and operation of the kind of schemes that have led to the Loan Charge.

The Loan Charge has failed to stop the promotion of disguised remuneration schemes

8. The reality is that the Loan Charge has been an abject failure in its avowed intention to stop the promotion and use of disguised remuneration schemes. We do not believe that the Government and HMRC have been held properly to account for this failure.

9. The reality is – as any web search will show – is that similar tax planning arrangements are still being promoted today. Many of these schemes are advertised as ‘legal’, ‘compliant’, ‘tax efficient’ etc and there remains the danger that people will unwittingly sign up to use these arrangements, and then find themselves with a large retrospective tax demand in the future. Indeed, the APPG are aware that public sector workers who have been impacted by the IR35 reforms may have been particular targets for promoters since 2017 and that workers in the private sector facing the 2021 IR35 reforms, are at risk of becoming the next significant market that such promoters will target.

10. In addition, Loans made directly by Employers to Employees are not within Part 7A of ITEPA 2003 – either as originally enacted or by the more recent legislative extensions. Current schemes being marketed appear to involve making direct payments, rather than doing so through a third party. Such schemes are not caught by Part 7A and therefore are not caught by the Loan Charge. This is yet more evidence that the Loan Charge was not the right, nor an effective solution to stopping the sale and use of tax avoidance schemes, as it doesn’t even apply to such schemes. It also is more evidence that the fundamental conclusion of the discredited Morse Review report (which has been shown not to be properly independent) that the “law was clear” from 2010/11 is simply not credible. It is time that the Government accepted this – and made the law clear around all such schemes.

11. So in light of the profound failure of the Loan Charge to achieve one of its main stated aims, to stop the promotion of such schemes, we do believe that much more action is needed from the Government and from HMRC and welcome plans to actually take the kind of action that has not been taken thus far.

HMRC's failure to pursue promoters of loan schemes

12. The reality, as exposed by Freedom of Information requests, is that there have been no arrests or prosecutions, never mind convictions, of anyone for promoting or selling the schemes that are now subject to the Loan Charge.
13. There has been a consistent and concerted campaign of disinformation by HMRC and the Treasury to give the false impression that HMRC have taken action against those who promoted the schemes which are now subject to the controversial Loan Charge, when this is not the case. HMRC (especially via their press office) have sought to give a highly misleading impression that they have taken action against loan scheme promoters, so much so that the APPG felt compelled to publish a report in March 2020 exposing this.
14. HMRC and the Treasury have admitted in an FOI response² that they cannot go after promoters of loan schemes as such schemes were not illegal and, ironically, the Financial Secretary to the Treasury has admitted that the government would need to change the law retrospectively to be able to do so.
15. The reality is that promoters of the schemes now subject to the Loan Charge have not and, it seems, will not face any action from HMRC for promoting the schemes. This is in stark contrast to those to whom they sold the schemes, and from whom they took large fees, some of whom are facing ruin as a result.
- 16. So we support moves to actually tackle those who promote and operate such schemes, but we also demand more honesty from the Government and HMRC in terms of presenting the outcomes of any action they do take or attempt to take.**

HMRC past failure to inform scheme users

17. One of the clear conclusions from looking at the evidence, as opposed to HMRC and Treasury spin, is that HMRC failed to warn scheme users that they did not approve of the scheme.
18. Inadequate communication from HMRC meant that many taxpayers were not informed about the Loan Charge until 2018 or 2019. The APPG Survey

² https://www.whatdotheyknow.com/request/loan_charge_information_provided#incoming-1336224

October 2019 showed that in some cases taxpayers have never been notified about the Loan Charge.³ Some users of schemes actually contacted HMRC and were not given any indication of any problems.

- 19. So we certainly support meaningful action by HMRC to “to contact customers early, where they have potentially entered into an avoidance scheme” as stated in the policy paper, but we want to hear more detail of how this will happen and how HMRC will ensure it learns the lessons from the Loan Charge Scandal.**

A key principle for action: The need to make promoters liable for tax avoided

20. The APPG believes that a simple principle should be adopted and introduced into law, that where HMRC demonstrates that a scheme is a form of contrived tax avoidance, that doesn't comply with legislation and the intent of Parliament, that those who operated such schemes should be the ones liable for tax avoided through it. We believe this is the simplest and clearest way to stop those seeking to profit from mis-selling dubious schemes. So we welcome the statement in the Government policy paper, “We want promoters to face the financial consequences of their actions with their financial risk more closely linked to the tax that their schemes are designed to avoid” and hope to see this enacted in a workable and effective way.

The possibility of using Managed Service Company (MSC) legislation

21. The Loan Charge APPG believe that the possibility of using Managed Service Company (MSC) legislation to tackle promoters should be properly considered by the Government. This is something that has been suggested to the APPG by tax advisers and something we agree should be explored.
22. MSC Legislation was introduced in Finance Act 2007, seeking to address identified gaps in the IR35 ‘intermediaries’ legislation and was a response to the proliferation and mass marketing of intermediary companies.
23. MSC Legislation allows for the liability for failure to pay the correct amount of tax to fall on the company, as the employer. In addition, the legislation MSC allows for a ‘transfer of debt’ from the MSC to ‘others’ including to directors, other office holders or associates of the Managed Service Company, but also to any other person who directly or indirectly has encouraged or been actively involved in the provision by the MSC of the services of the individual, or a director, or other office holder or associate of such a person.

³ <http://www.loanchargeappg.co.uk/wp-content/uploads/2019/04/Loan-Charge-APPG-Loan-Charge-Inquiry-Survey-Report-March-2019.pdf>

24. If applied to all umbrella companies/umbrella schemes, the same thing could (if the legislation is drafted properly and definitions are clear) could allow HMRC to pursue such companies and the individuals behind them and involved with them. This would then put those operating schemes at the risk of being pursued and being personally liable, as their clients/customers currently are. If their own assets were at risk, then we believe this would make the marketing and operation of such schemes too risky. So the view of the APPG is that the only clear way to stop the continued marketing of dubious schemes is such a transfer of liability/debt. So extending this to umbrella company/schemes would, we believe, stop the majority of scheme promotion in this area.

The need to properly clarify the law around 'tax avoidance'

25. Tax evasion is illegal, whilst 'tax avoidance' is not, nor is it actually defined in law (despite the Government's attempts to present it as an identifiable concept in policy terms).
26. HMRC and Ministers routinely use the phrase "doesn't work" which has no basis in law. **So we suggest that the law may need to be changed so that it is clear what is regarded as legitimate tax planning and what is regarded as illegitimate tax planning.** This would avoid the grey area that has been produced, whereby some ways of seeking to minimise tax bills are deemed legitimate and others are not. The law must be clear, so that such matters are not left to the judgment of HMRC and politicians, but are properly defined and understood in the law.
27. Whilst it may be appropriate to pursue some promoters of schemes using criminal investigation (and should certainly be done in cases of suspected tax evasion and any cases involving suspected fraud) we do not believe that this is the solution to clamping down on the promotion of schemes, as it is unclear what criminal offences may have been committed and this could become clear if the law was properly clarified. As it is, fraud cases are notoriously difficult to successfully prosecute (even where the fraud is clear) and hugely expensive to pursue, which is one of the reasons so many cases do not proceed to trial, **so we believe that shifting the tax liability onto operators of schemes, should they be deemed as unacceptable tax avoidance, is the best way to tackle the ongoing promotion of such schemes. Such a liability should be passed onto directors of companies who operate any such scheme.**

Regulation of umbrella companies/schemes

28. The Loan Charge APPG are clear that when operated properly and ethically (and where tax is paid as it should be), umbrella companies can be a

legitimate way of working, for contactors and freelancers, particularly in the light of the IR35 off-payroll working rules.

29. However, we believe that such companies now need to be properly regulated (through statutory means) to stamp out the misuse of such companies for the purposes of marketing and operating tax avoidance schemes. We do not believe that considering the misuse of umbrella schemes/intermediaries, that non-statutory regulation would be effective. We believe that the reputable operators of such would welcome this, to allow them to continue to offer a legitimate service and structure to freelance workers.

An underlying fundamental problem – the lack of a definition of ‘contracting’, ‘freelancing’ and ‘self-employment’

30. Whilst we support the fact that the Government and HMRC are finally admitting that thus far, their attempts to close down tax avoidance schemes have been generally ineffective and that promoters still operate openly, which they intend to tackle, we are also concerned a fundamental issue is not being tackled of how to recognise and tax self-employment, contracting and freelancing. The Government’s approach is contradictory and at the same time as wanting to clamp down on tax avoidance schemes, they are simultaneously introducing legislation that they have been warned, by experts and professional bodies, will likely lead to more tax avoidance schemes.
31. Much of the problem goes back to the flawed ‘IR35’ legislation (something highlighted by the Economic Affairs Committee in their powerful report Off-payroll working: Treating people Fairly, published on 27 April 2020). This legislation has placed additional tax liabilities on genuine freelancers and contractors, including employer’s National Insurance Contributions (NICs). As a result, many genuine contractors faced the risk of tax bills that exceeded those of any Pay As You Earn (PAYE) employees, whilst having none of the 10 associated benefits and protections under employment law.
32. Despite the strong recommendation of the Committee, professional bodies and many Parliamentarians (and considerable evidence of the damage this change is causing) the Finance Act is rolling-out the IR35 ‘off-payroll working rules’ to the private sector in April 2021.
33. What is really needed is to align tax law with employment law and to properly define what is meant by self-employment, in its different forms including contracting and freelancing and then come up with a sensible and fair system for recognising and taxing such forms of working, acknowledging that such working structures do not constitute employment nor do they receive the security and benefits of employment. If the Government does not

want contractors and freelancers to use Limited Companies, it needs to be clear how freelancer and contractors should operate. We hope it will do so, in the proposed review into self-employment, as proposed in the Conservative General Election 2019 Manifesto⁴.

The danger of giving any more powers to HMRC without proper consideration and scrutiny

34. As a wider point, whilst we support and have called for changes to the law that clamp down on the promotion of tax avoidance schemes. We would be very concerned about HMRC being given any more powers, as the experience of the Loan Charge shows that they misuse these powers, are largely unaccountable and are not properly overseen by the Treasury nor subject to proper scrutiny. The disturbing way HMRC have behaved towards people facing the Loan Charge (and their advisers) was covered in a report published by the APPG in June 2019. So currently, there are insufficient safeguards to ensure an appropriate balance is struck between HMRC and taxpayer and this needs addressing. This point was also made by the Economic Affairs Committee in the report, *The Powers of HMRC: Treating Taxpayers Fairly*. Such concerns must be part of the consideration of granting any further powers to HMRC and any new powers must be accompanied with proper checks, balances and scrutiny.
35. A combination of factors, including the merger of the Inland Revenue and Customs and Excise; the cuts to HMRC's budgets, the increasing pressure from politicians to clamp down on tax avoidance/collect missing tax and increased powers given to HMRC, has led to HMRC becoming far too focused on aggressively pursuing tax without consideration of the human or financial costs of doing so.
36. We are also concerned about the relationship between the Treasury and HMRC. The Treasury, as the Ministerial Department, is supposed to oversee HMRC and take responsibility for issues and failings. Instead, Treasury Ministers, who are supposed to oversee HMRC, instead act as spokespeople for HMRC, ignore HMRC wrongdoing and routinely share HMRC press lines and propaganda, including in responses to Treasury questions. The Economic Affairs Committee itself has criticised Ministers for the way they ignore scrutiny.
37. We are also concerned at the clear and direct influence of HMRC on policy-making, when policy-making should be conducted by the Treasury. It is clear that the Loan Charge was conceived within HMRC as a way of dealing with the

⁴ *Get Brexit Done, Unleash Britain's Potential*, The Conservative and Unionist Party Manifesto 2019, page 34 https://assets-global.website-files.com/5da42e2cae7ebd3f8bde353c/5dda924905da587992a064ba_Conservative%202019%20Manifesto.pdf

fact that they had missed their chance to pursue many individuals, where they had failed to open enquiries when people had used loan schemes. There is a need for much more transparency on HMRC as part of a new system of oversight and scrutiny.

38. What is urgently needed overall is an effective system of scrutiny of HMRC, with proper Parliamentary scrutiny and independent oversight. We believe that this is essential, alongside creating a framework where the Government HMRC can legitimately and properly both close down unacceptable tax avoidance schemes and pursue those behind them.

Conclusion

39. The Loan Charge APPG supports the introduction of effective measures to clamp down on the ongoing marketing and operation of unacceptable tax avoidance schemes, however we need to see the detail and further information about how measures will work in practice. We believe that the key principle for meaningful action is to pass the liability for any tax deemed to have been avoided onto the company operating any such scheme and the individuals involved in it.
40. We also believe that such measures must also be accompanied by a much needed new system of scrutiny and oversight of HMRC, to also address the worrying way HMRC operates and the risk to vulnerable UK citizens as a result. We also urge the Government to finally and properly address the need for a proper definition of self-employment, contracting and freelancing and for this to be recognised in law. It needs to be clear how such working practices should be structured which in itself would close down the market for those offering and mis-selling structures and arrangements that are unacceptable and could lead to those using them (and victims of mis-selling) being hit by huge retrospective tax bills.

7th October 2020