

The 5 April 2019 loan charge – Part II

(Lecture P1084 – 8.01 minutes)

PAYE

5 April 2019 is the trigger date for PAYE so tax must be accounted for in the April payroll run and paid by 22nd of that month. Well, that's the theory.

However, bearing in mind that PAYE must be deducted with nothing to deduct it from (these are deemed earnings not real wages), the employer will be left in the unenviable position of coughing-up the PAYE and then trying to recover the tax and NIC from the employee. This is hard enough if the employee is still on the premises (and next to impossible if not).

To apply PAYE correctly, the employer will need details of the amount outstanding. The new loan charge provisions therefore include a requirement that both the person who made the loan (ie, the third party) and the employee who received it must provide information about the loan balance to the employer who is to operate PAYE.

All individuals who have received a loan from a disguised remuneration scheme must provide HMRC with contact details, HMRC references, and details of the outstanding balance of the loan (including any amounts already written-off) no later than 1 October 2019. This will enable HMRC to identify all employers on whom a PAYE obligation falls and will no doubt trigger collection notices under the PAYE Regulations in due course.

If the employer is not compelled to operate PAYE (for example by having no UK tax presence) or if the employer no longer exists, the employee will need to include the value of the relevant step in his 2018/19 Self-Assessment and pay the tax by 31 January 2020. In this case there is no Class 1 NIC liability.

If the employer has a UK presence and still exists but is simply unable to pay, the tax liability can be transferred out to the employee by HMRC applying its existing powers under the PAYE Regulations (Reg 81). As Regulation 81 only applies in relation to tax, there would be no Class 1 NIC liability transferred over to the employee.

This will have the inevitable knock-on effect of many employees not having the means to pay the tax without selling off assets such as their homes. The more hard-nosed amongst us will no doubt argue that these people may not have been able to afford these assets if they (like the rest of us) had paid income tax and NIC on their employment income in the first place, so a clawback is justified and long overdue. What do they say about things which seem too good to be true...?

It is hoped that HMRC will be reasonable in setting up time-to-pay arrangements and agreeing repayment plans with affected employees and indications are that they will. Some of the affected employees will however be forced into IVAs or bankruptcy.

Accelerated Payments Notices (APNs)

HMRC's victory at the Supreme Court in the protracted and much publicised Rangers case in July 2017 has certainly put a great deal of wind in HMRC's sails and this momentum will be hard to stop.

Buoyed by the Rangers victory, HMRC used their September 2017 (Edition 41) of Spotlight (“Disguised remuneration: A Supreme Court decision”) to reiterate that:

- Employment income paid from an employer to a third party is still taxable as employment income; and
- This principle applies to a wide range of disguised remuneration tax avoidance schemes, no matter what type of third party is used (including but not necessarily limited to EBTs, EFRBS and a range of contractor loan schemes).

The Supreme Court in Rangers upheld HMRC’s long-held opinion that payments from the employer to the EBT were taxable as employment income. So, if this is now the established position, is the 2019 Loan Charge unnecessary?

The wheels for the Loan Charge were already in motion well before July 2017, presumably on the basis that HMRC expected to lose in Rangers (having failed to convince the courts of this point at their previous appeals) and HMRC were therefore putting in place an alternative statutory weapon in their fight against these schemes. Their subsequent continuance with the Loan Charge in the wake of Rangers is “belt and braces” and an extra stick to beat us with. I guess that, as with any decided case, the danger is that taxpayers will argue that the facts in Rangers don’t sit 100% square with their own so the decision does not apply. After all, in Rangers the employer sent a letter to the EBT Trustees asking them to resettle the funds on sub-trusts for the employee to call on as he pleased. The Loan Charge is therefore the government’s safety net.]

Spotlight 41 promised that HMRC would use the Rangers decision “to take action against many of the disguised remuneration schemes using the full range of our available tools”. This in turn has been the catalyst for a raft of Follower Notices and APNs in relation to EBT schemes.

Some taxpayers who are potentially subject to the April 2019 loan charge will therefore already have paid tax in relation to their outstanding loans under an APN (issued either in relation to a loan-scheme notifiable under DOTAS or after the issue of a Follower Notice pursuant to cases like Rangers). Taxpayers who have made a payment under an APN in respect of the 2019 loan charge can apply to postpone the loan charge payment date but only if that payment is equal to or more than the outstanding loan balance. Applications for postponement must be made by 31 December 2018.

If the loan charge exceeds the APN payment, the APN payment (being a payment on account) can be used to offset any liability due at 5 April 2019.

What now?

Firstly, if you have clients with a possible Loan Charge exposure, the sensible advice is to speak to a specialist with experience in this area and with clients in the same boat. This is not an area where one can Google and go from there.

Taxpayers faced with an April 2019 loan charge have a few options.

Ignore it and hope it all goes away. It won’t. So don’t. HMRC has a habit of finding out about these things and have a population of people employed for this purpose (plus having this particular skeleton in one’s closet can’t be good for the blood pressure).

Ignoring it leaves the way open for increased penalties for non-disclosure (and in cases where the loan is from an offshore scheme, the penalties could fall to be levied under the stricter rules for offshore tax evasion which can lead to Magistrate appearances and jail-time). We will therefore rule this out as an option.

Repaying the loan vs. Paying the tax:

This is an interesting choice.

Let's say your client (X) has outstanding EBT loans of £1 million. If X does nothing, the loan charge will hit in 2018/19 and X will have to pay c. £450,000 in income tax in January 2020. X has until then to raise the money (which should be plenty of time).

Or X could repay £1 million to the Trust before 5 April 2019 (which will cost him more and gives him less time to raise the cash). Prima facie the choice seems obvious. Except....

If X repays the loan, the money will sit in an offshore EBT earmarked for X's benefit thereby giving him (subject to the discretion of the usually cooperative Trustees) access to that money going forward. OK, chances are that if the Trust pays that money to X, the amounts paid will be charged to income tax. However, it might be possible to limit or control the liability either by arranging payments to non-resident beneficiaries outside the UK or by waiting until retirement and dripping out the money to use X's allowances and basic rate bands. We should therefore think of the loan repayment as akin to a contribution to a pension fund whereby money is put aside now to access in the future as the need arises.

Alternatively, the Trustees could be persuaded to invest the fund in a mutually beneficial commercial venture - say X's new business in the UK? - without creating a tax charge.

As an aside, the offshore EBT will be a discretionary trust, so if the money is repaid to the Trustees it will sit outside the individual's estate for IHT. Strictly this will mean that the trust is also a relevant property trust and liable to exit and periodic charges but quite how compliant offshore EBTs have been with those rules is anyone's guess.

Settle the case with HMRC before 5 April 2019:

Settlement means accepting that all funds paid to the third party (EBT) on behalf of the employee are taxable as employment income (which has always been HMRC's stance and which was confirmed in *Rangers*). This avoids the loan charge as HMRC has generously confirmed that they have no desire to try and tax the same money twice. It also avoids the need to repay the loans as the loans will no longer be loans from a tax perspective. But it will still cost money.

HMRC has historically preferred the settlement route. To facilitate this employers and employees were presented with the opportunity to register their interest in settlement by 31 May 2018 with a view to taxpayers providing all relevant information by 30 September 2018 and settling their liabilities before the loan charge hits in April 2019.

For those who have registered their interest, a negotiated settlement may turn out to be the cheapest way of resolving the issue because the tax liability will be calculated on a year-by-year basis thereby using the rates and bands for the years in which the loans were taken out.

The amount taxable will be the employer contribution to the EBT, less any fees incurred for that purpose. Once this calculation is performed, any amounts previously charged to tax under the beneficial loan rules will be deducted and credit given for tax paid on those benefits, but (it seems) only for those years that are still under appeal (although there may be room to claim overpayment relief subject to the relevant time limits).

The settlement will be required to include tax for those years which may be out of time for a discovery assessment, these being included in the deal as “voluntary restitution” on the part of the taxpayer (which is jolly decent of him).

The settlement will include interest for all “in-date” years (but not for tax which is paid “voluntarily”).

A CT deduction will then be available for the employer contributions to the EBT – these now being matched with a charge on earnings – but only for CT returns which are still open or still within time to be amended.

For those who did not register an interest by 31 May, strictly speaking the settlement route is now closed. However, HMRC have quietly extended this to 30 September 2018 so registration is still possible for those clients who have only recently come to the decision to settle.

Is the Loan Charge fair?

Many, including our elected representatives, think not.

An Early Day Motion (EDM1239) was tabled in the House of Commons on 8 May 2018 (and has over 50 supporting cross-party MPs) which lists many concerns about the April 2019 loan charge including:

- that it is retrospective applying back to 1999;
- because of the introduction of IR35, umbrella companies were set up and recommended by professional advisers... and that this Charge will affect contractors, freelancers and agency workers, including social workers, supply teachers, locum nurses and doctors;
- it is unfair that HMRC are pursuing people who acted in good faith rather than the client organisations, agencies or umbrella companies all of whom benefited significantly;

HMRC are aggressively pursuing individuals through Advanced Payment Notices with no independent right of appeal:

- the Charge is likely to cause financial distress and bankruptcies, impeding HMRC's ability to recover these tax liabilities and causing a devastating impact on people; and
- that retrospectively taxing something that was technically allowed at the time, is unfair.

The Motion concludes by “calling on the Government to revise the legislation to avoid significant damage to independent contractors and freelancers in the UK”. Fine words indeed. But we seem to be way too far down the line with this for there to be any significant back-peddalling so this motion will probably fall on deaf ears. But we will let you know if it doesn’t.

Contributed by Steve Sanders