HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ

All-Party Parliamentary Loan Charge & Taxpayer Fairness Group
Office of Sammy Wilson MP
House of Commons
London, SW1A 0AA

28 February 2022

Dear Sammy, Greg, Mohammad, and members of the All-Party Parliamentary Group,

Thank you for your letter of 3 December 2021 and your continued engagement on this important issue. I would also like to thank you for taking the time to meet with me on 15 December 2021. I found our meeting very helpful.

In our meeting, I committed to provide a response to your specific concerns. I have taken the time to read the legislation and the Independent Loan Charge Review, consider the outcomes of the legal challenges to the Loan Charge, and discuss the policy with officials.

As you are aware the reason the Loan Charge was introduced was to ensure fairness for all taxpayers, including those who did not use disguised remuneration (DR) schemes. That principle remains important – because it would be unfair for two taxpayers in the same circumstances to pay different rates of tax.

I note that in Cartref (and others) v HMRC the judge stated at para 225: "The purpose of the legislation is not one that can be sensibly impugned; it is to deprive tax avoidance schemes of oxygen, and to ensure that people and companies bear their fair burden of tax, rather than throwing unfair weight on others – in particular those who do not have the opportunity to use such schemes. The legislation is rationally connected to its objective."

As you know DR has a long history. There have been a significant number of cases heard by the courts and issues have been raised with a number of successive Treasury ministers, with a statement made by the minister to Parliament in 2004 warning that the Government would take action to bring DR avoidance to an end. Legislation was introduced over 10 years ago to specifically address DR schemes and the Loan Charge was announced in 2016 to draw a line under the use of DR schemes. The Loan Charge has been the subject of an independent review and the Government has successfully defended every legal challenge brought against it to date. The Government does not intend to reopen consideration of the Loan Charge.

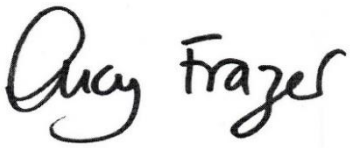
I recognise the impact that the Loan Charge can have on individual vulnerable taxpayers who are not able to pay and who are deeply affected by the charge. I understand from HMRC that vulnerable individuals are supported on a case by case basis and that all HMRC compliance teams are trained to identify those customers who may need extra help, including those in distress, and to ensure that every customer receives the help they need. This may be through support that HMRC can provide, or by signposting to other specialist organisations, such as Mind or the Samaritans. I continue to explore that work and I hope to work closely with you on any further support it might be appropriate to offer to those who may need it.

On the specific points you raised, I am replying to you as the minister responsible for the Loan Charge policy, and not in my capacity as a lawyer. While it is unusual for a minister to comment on the application of tax statute and court cases in any detail, I recognise your concerns and want to reassure you that the Government's position is legally robust. For those reasons I have attached a response from HMRC which answers the questions you have raised in detail.

I have received and thank you for your letters of 19 January 2022 and 7 February 2022; I will respond to you shortly on that correspondence and I look forward to meeting with you again to discuss how support can best be provided to those affected.

I look forward to responding to your further correspondence and meeting you again soon.

Yours sincerely,



THE RT HON LUCY FRAZER QC MP

Annexe

Questions 1 & 2

1. The Government has successfully defended every legal challenge brought against the introduction of the Loan Charge.

2. Lord Morse concluded that from 2010 it was clear that DR schemes did not work because at this point the introduction of anti-avoidance legislation at Part 7A of the Income Tax (Earnings and Pensions) Act (ITEPA) 2003 put HMRC's longstanding position on employment related DR schemes beyond doubt. The changes made to the Loan Charge by the Government following the Review mean that loans made before 9 December 2010 are no longer in scope.

3. Following the legislation new forms of DR schemes were introduced which were claimed to avoid income tax, including self-employed or trading income schemes and schemes where loans are made directly by an employer rather than via a third party.

4. The Loan Charge does not apply where disguised remuneration loans are made directly by an employer to an employee, unless the rights to repayment are transferred to a third party, though they are taxable as earnings and are subject to PAYE. The Review therefore did not consider this scenario.

5. For self-employed or trading income schemes, the tax law requires that the starting point for calculating trading profits is Generally Accepted Accounting Principles (GAAP), which are not prescribed by HMRC. These principles require the calculation of profits to reflect the substance of transactions, which may differ from their legal form. Once the profits are calculated under GAAP they may be subject to adjustment under tax law, for example, an expense may not be tax deductible if it is capital in nature, or if it is not incurred wholly and exclusively for the purposes of the trade. The relevant accounting principles and tax law in this area are clear, longstanding, and pre-date December 2010.

6. In 2017 new anti-avoidance provisions were introduced at ss23A-H of the Income Tax (Trading and Other Income) Act 2005 to clamp down on future use of self-employed schemes and reduce the time and resources deployed in challenging schemes under pre-existing accountancy principles and tax rules. Those new sections supported the introduction of the self-employed Loan Charge, as the Loan Charge operates by reference to those provisions as if they applied prior to 2017.

7. The most notable judgement on DR is in the 2017 Rangers case, where the Supreme Court confirmed the principle that income paid from an employer to a third party in respect of services provided by an employee is still taxable as employment income of the employee. The Supreme Court also held that previous adverse decisions which concluded that income tax was not due were either wrongly decided by the lower courts (Sempra Metals v HMRC) or the Supreme Court disagreed with their conclusions (Dextra Accessories v HMRC). HMRC has also successfully challenged contractor DR use at the First Tier Tribunal.

Question 3

8. It is not unusual for the end user of a contractor's services or their agency to be unaware that the contractor was participating in an avoidance scheme. In these cases HMRC may collect tax from the contractor using provisions made available to it by Parliament. Section 684(7A) of ITEPA 2003 is one example of such a provision. This puts the contractor in a comparable position to any other employee who would, in the normal course of events, have had tax deducted from their income by their employer and paid to HMRC.

Question 4

9. The requirement for an employer to account for PAYE does not supersede or eliminate an employee's liability to tax. As explained previously, the person liable for tax on employment income is the person to whom the earnings relate. The tax statute (section 13 ITEPA 2003) referred to in the 2017 Rangers judgement says that the person liable for tax on employment income is the 'taxable person', who is the person to whose employment the earnings relate. The purpose of s684(7) is to enable the PAYE provisions to place an obligation to operate PAYE on an employer when they make a payment of PAYE income to an employee, despite the fact that section 13 places liability for the tax on that income on that employee. The two provisions work together to allow PAYE to be operated by the employer whilst maintaining the employee's ultimate liability for the tax due and, importantly, to support the further provision which confirms the employee's right of appeal in relation to an amount of taxable income. Without an employee having an earnings liability, it would not be possible to conclude that the employer has a PAYE obligation. Section 684(5) confirms that nothing in the PAYE regulations affects an employee's right of appeal. This needs to be included because liability for any tax due remains with the employee.

10. Rangers did not address the provisions that result in an individual being required to pay their tax direct to HMRC as it was not relevant to the particular case. However, Lord Hodge is clear in the judgment that when payment is routed through a third party, the PAYE system can operate without difficulty. The PAYE system includes provisions which allow HMRC to collect tax from the employee, but this is subject to the relevant conditions being met. Any taxpayer who disagrees with a Loan Charge assessment can appeal to the First-tier Tribunal.

Question 5

11. It would not be appropriate to comment on ongoing legal matters, including the Upper Tribunal's decision in Hoey v HMRC, which has been appealed to the Court of Appeal. The use of provisions or discretion in the PAYE system to collect tax from individuals is an operational matter for HMRC.

Question 6

12. You have also asked about HMRC's efforts to tackle promoters. A key part of HMRC's strategy in tackling promoters of disguised remuneration and other tax avoidance schemes is to change their behaviour so that they stop this activity altogether. HMRC has a range of legislative powers to tackle promoters, under three main regimes: Disclosure of Tax Avoidance Schemes (DOTAS), Promoters of Tax Avoidance Schemes (POTAS), and the Enablers penalty. Penalties can be charged for various failures to comply with the requirements of these regimes. Fewer than five penalties have been charged under DOTAS by the Counter-Avoidance team since 2013. Before then a further 11 penalties were charged for more historic DOTAS failings. Giving further details of the penalties would

potentially lead to a disclosure of confidential taxpayer information which is prohibited by section 18 of the Commissioners for Revenue and Customs Act 2005. These regimes have had a positive impact in changing the behaviour of some promoters, with a number of promoters either stopping selling or ceasing business altogether. Over 20 promoters have left the market since 2014; the majority of these promoted DR schemes. HMRC has successfully litigated several cases involving promoters who failed to comply with their obligations under DOTAS.

13. Promotion or operation of mass marketed tax avoidance schemes is not in and of itself a criminal offence. However, there are a range of offences which might be committed by those who promote tax avoidance schemes or advise on their use. On that basis, to date, while there have been no prosecutions of individuals directly related to the promotion of schemes subject to the Loan Charge, a number of individuals are currently under criminal investigation by HMRC for offences linked to schemes subject to the Loan Charge.

14. To ensure fairness to taxpayers, the Government strengthened HMRC's powers to tackle promoters in Finance Act 2021 and is bringing forward in Finance Bill 2021-22 a further tough new package of measures to tackle promoters of tax avoidance.

Question 7

15. Between 2009 and 2019 Lord Morse was the Comptroller and Auditor General of the National Audit Office and he has a strong record of holding the Government to account. He had full discretion over how the review was run, which stakeholders he engaged and the recommendations he made. The Review report explains that "over 700 personal testimonies and contributions from 37 tax and legal experts" were considered alongside "evidence provided in meetings following external consultations with stakeholders". The Government accepted 19 out of the Review's 20 recommendations, and these were put on a statutory footing where necessary in Finance Act 2020.

Question 8

16. Your letter asks about the legal rights and statutory time limits which apply to all taxpayers. The Loan Charge does not change any taxpayer safeguards, including time limits or rights of appeal. It is a new tax charge which applies to DR loan balances outstanding on 5 April 2019 and does not change the tax position of any previous year. Taxpayers have the right to appeal tax decisions made by HMRC and where someone disagrees with HMRC's assessment that the Loan Charge applies they are able to appeal that decision.

Question 9

17. You have also asked about the scheme to repay Voluntary Restitution payments. HMRC has written to around 2,000 customers it identified might be eligible for a repayment or waiver, inviting them to make an application. By the September 2021 deadline, it had received around 2,460 applications for a refund. As of 28 January 2022, HMRC had processed approximately 1500 applications, of which around 1000 had received either a repayment, a waiver, or both. Approximately 500 of the applications processed at that date were either invalid or ineligible.

18. HMRC checks several criteria to determine whether someone is due a repayment or waiver and several other criteria before it reviews whether a customer has made a reasonable disclosure. There may be taxpayers who made a reasonable disclosure but were found to be ineligible for a repayment or waiver for other reasons before the reasonable disclosure criteria was fully considered.

19. HMRC recognises the importance of processing repayments quickly and accurately and is working hard to process the applications it has on hand as quickly as possible. HMRC received more applications than expected and some repayments involve complex calculations that will take longer to complete.

Question 10

20. This question has been addressed in the letter above.