



HM Revenue
& Customs

Extension of the existing security deposit legislation to include CT and CIS deductions

Summary of Responses

6 July 2018

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1. Introduction

Background

- 1.1 At Autumn Budget 2017, the government announced that it would extend existing security deposit legislation to include corporation tax (CT) and Construction Industry Scheme (CIS) deductions from April 2019, and consult on the most effective way of introducing this change.
- 1.2 The consultation document “*Extension of existing security deposit legislation to include CT and CIS deductions*” was published on 13 March. Comments were invited by 8th June 2018.
- 1.3 The consultation set out how the existing security regime operates and the circumstances, where there is a serious risk to the revenue, in which HMRC may seek a security. It also explained how the use of securities is carefully targeted at those who won’t, rather than can’t, pay the tax that they owe, and set out the procedural and legislative safeguards that are in place to protect the taxpayer.
- 1.4 The consultation proposed that the securities provisions for CT and CIS deductions should follow the existing regime as closely as possible. It suggested that CIS, which is very similar to PAYE in its structure, would fit quite easily within the existing model, but recognised that the profits-based nature of CT might require a slightly modified approach. Respondents were invited to comment on the proposed operation of the new securities and how the offence for not complying with a security notice might be framed.

Consultation Responses

- 1.5 We are grateful to those who responded to the consultation. We received 5 written responses and have had helpful discussions with some interested parties.
- 1.6 Chapter 2 of this document sets out the reaction to the consultation and the government’s conclusions.
- 1.7 Chapter 3 of this document outlines the next steps in respect of this measure.

2. Responses

General comments

- 2.1 All respondents agreed that HMRC should be able to deal effectively with defaulters that pose a serious risk to the revenue but opinion was divided on whether in principle the existing securities regime should be extended. Some respondents felt that HMRC should use existing powers to take action against those that abuse the tax system.
- 2.2 It was acknowledged that the target population for securities was small but concerns were raised that some companies in genuine distress might be caught. All respondents emphasised the importance of rigorous safeguards and an appropriate appeals mechanism to ensure fairness to taxpayers.
- 2.3 Most respondents wanted to see clear guidance put in place to support the introduction of the securities and ensure that securities will only be used where it's appropriate and proportionate to do so. Two thought that legislation should be expanded to provide the rules under which the securities regime should operate.
- 2.4 Several respondents commented specifically on the implications for insolvency and commented that HMRC should give careful consideration in cases where viable businesses were struggling financially and a security could force the business into insolvency. Similarly, respondents did not want the use of securities to limit the rescue environment for financially distressed businesses. One respondent suggested that before extending the security deposit regime, HMRC should commission independent research into its current approach and the effect that demands for a deposit have on struggling businesses.
- 2.5 Several respondents also noted that if a security was taken from a business that subsequently becomes insolvent, whilst this could help HMRC reduce its losses it would be to the detriment of other creditors.

Responses to consultation questions

Question 1: Do you think there are any further forms of security that could be provided?

- 2.6 Under existing powers, HMRC accepts security deposits as cash payments or as a guarantee in the form of a performance bond issued by a financial institution. The consultation invited views on whether there are any further forms of security that might be appropriate in this context.

- 2.7 Those who responded to this question agreed that the current options were sufficient. The government therefore intends that CT and CIS securities will be payable by cash or performance bond, in line with current practice.

Question 2: Do you agree that any company within the scope of the charge to CT should fall within the scope of the CT securities provision?

- 2.8 The consultation proposed that the scope of the CT security provision should be framed broadly and include any company that falls within the charge to CT, where HMRC believes there is a significant risk to the revenue relative to the size of the company.
- 2.9 Several respondents questioned whether it was appropriate to extend securities to CT at all, as struggling companies would be unlikely to have significant CT liabilities and the level of CT debt would be small. One respondent supported the use of securities in cases of abusive phoenixism but noted the need to exclude from the scope of the measure the legitimate sale of a business or assets to maximise the return to creditors out of an insolvent situation.
- 2.10 The government recognises that the use of securities should be carefully targeted. As at present, HMRC will consider all securities on a case by case basis, taking full account of the business's circumstances and will only seek securities where it is reasonable and proportionate to do so. Whilst the government intends the legislation to follow the approach proposed in the consultation, it considers that certain types of companies will be unlikely to require security action in practice (such as companies that pay tax in advance under the quarterly instalment payment regime). It also notes that most companies that fall within the charge to CT will never be affected by this measure.

Question 3: Do you agree that it's reasonable to estimate the amount of CT revenue at risk by reference to taxpayer provided information and wider sources of relevant information, including HMRC data, or are there other ways in which the amount of security could be calculated?

- 2.11 Several respondents thought that quantifying the CT liability for the purposes of a security requirement would be more challenging and resource intensive for HMRC than for VAT or PAYE, due to the nature of the tax. One respondent thought that where quantification was required it would be reasonable to work with the company to establish the potential tax at risk, as an estimate based on similar types of business was not appropriate given there could be significant differences in how they operate. This respondent also noted that the proposed reporting requirements under making tax digital could have a positive impact on HMRC's ability to assess a future tax liability on account that HMRC would be receiving information more regularly.

2.12 The consultation acknowledged that a modified approach will be required to assess the amount of future revenue at risk for a profits-based tax and suggested that HMRC officers would draw on relevant information and seek input from the company in order to estimate the company's potential tax liability and revenue at risk. There is precedent for this approach in our current securities process and other areas of the business; for example, when HMRC issues determinations in the absence of a tax return. The government has concluded that this is a reasonable approach, but it will ensure that adequate safeguards are in place through review and appeals procedures to allow the company to challenge the amount of security required.

Question 4: Do you agree that allowing payment in instalments or using a series of securities staged over a longer period could offer a way of balancing the protection of the revenue at risk with reducing the financial impact on the company? Are there any other approaches that you consider would be helpful in establishing an appropriate balance?

2.13 Only two respondents specifically addressed this question. One thought that if a company was unable to pay they should not be subject to the security provisions at all, and alternatives, such as time to pay arrangements should be considered. The other respondent felt that time to pay would be inappropriate in cases of abusive phoenixism because this would undermine the effectiveness of requiring a security.

2.14 In the absence of any clear support for this proposal the government does not intend to introduce specific provisions for staged payments. HMRC may consider applications for time to pay a security on a case by case basis, under their existing management powers and operational approach.

Question 5: Do you think there should be a simple offence of failing to provide a security when required, or is there an alternative approach that would be suitable for CT?

2.15 One respondent commented that HMRC already had means of penalising companies that don't meet their tax liabilities and that failure to provide a security should not be a criminal offence due to the difficulties in quantifying a CT security. Another supported the proposed simple offence where CT securities were targeted at abusive phoenixism.

2.16 The government has considered carefully whether a criminal power is necessary and has concluded, on evidence from the existing regime, that the effectiveness of securities relies upon the existence of a criminal sanction. For PAYE and NICs, there is a simple offence of failing to provide a security within a specified period and the government intends that the offence for the failure to provide a CT security will mirror this approach.

Question 6: Do the proposed safeguards strike the right balance between protecting the taxpayer and tackling the behaviour of deliberate non-compliance?

- 2.17 Most respondents commented generally on the need for strong taxpayer safeguards and rights of appeal, and some commented that appeal arrangements should not involve a business incurring additional costs.
- 2.18 One respondent questioned whether the proposed safeguards would be effective in view of the way in which CT is calculated and the greater difficulties in quantifying the amount of tax at risk. It was suggested that HMRC might consider having a panel to oversee the application of the regime, to ensure consistency of approach and proper targeting of the provisions.
- 2.19 The government recognises that a requirement for a security, underpinned by a criminal offence, is a serious measure, and robust taxpayer safeguards are required to ensure that securities are targeted and proportionate. The government considers that the appeals provisions in the Income Tax (Pay As You Earn) Regulations 2003 provide a suitable model for CT, and intends that the CT provisions will include similar rights of appeal to HMRC and/or a tribunal against the issue of a notice of security or any requirement in it.
- 2.20 There will also be provisions for a person who has paid a security to apply for a reduction in the amount if changes in circumstances mean they are no longer a person from whom security can be required, or the amount of security held by HMRC is no longer proportionate to the risk to the revenue. This will be particularly relevant in the context of CT, where the future revenue at risk is potentially more changeable. It is intended that a tribunal will have the power to confirm, vary or set aside the requirements in a security notice, and to confirm or vary HMRC's decision in respect of any application for a reduction in the amount of security.

Question 7: Do you think the proposed scope of CIS securities targets the measure appropriately?

- 2.21 Some respondents agreed, in principle, that HMRC should be able to require a security from any person that is required to register as a contractor under the CIS, where HMRC reasonably believes there is a risk of non-payment of CIS deductions. This would be subject to HMRC continuing to distinguish those who cannot pay from those who will not pay.
- 2.22 Other respondents commented that CIS has many existing reporting requirements and penalties for not complying with the regime and thought that the focus should be on improving the operation of CIS, including the online system, before including CIS within the securities regime. They also suggested that there was a potential for securities to influence the market if they led to contractors only employing subcontractors with gross payment status, because of a perception that HMRC might require a security.

- 2.23 One respondent noted that where a contractor was also a subcontractor, the withdrawal of gross payment status could already provide an effective sanction. It was also noted that securities would have limited effectiveness if contractors were not resident in the UK.
- 2.24 Two respondents commented that the CIS system was often slow to repay where a company is due a refund, and thought this should be addressed if securities are extended to CIS.
- 2.25 The government notes the comments received but considers that it is legitimate for HMRC to take a tough approach against those who deliberately abuse the insolvency rules. It is appropriate for HMRC to be able to seek a security in cases where this is necessary for protection of the current and future revenue. Therefore, the government intends that HMRC shall be able to seek a security from any person who is, or may be, liable to make tax deductions from payments to subcontractors, and accountable for paying these amounts to HMRC.

Question 8: Do you agree that it should be an offence for a payment to be made to a subcontractor when a requirement for a security has not been met or is there an alternative approach that would be more suitable?

- 2.26 Several respondents had concerns that the suggested approach would impact detrimentally on the supply chain and could leave subcontractors unpaid for work undertaken, resulting in financial distress to third parties. Two respondents also commented that given the similarities between CIS and PAYE, it was sensible for the offence for not complying with a security deposit for CIS to mirror that for PAYE and NICs.
- 2.27 The government has given further consideration to this point in the light of these comments and accepts the argument for consistency with the approach used for PAYE and NICs. Therefore, for CIS securities there will be a simple offence of failing to provide a security within a specified period, based on the existing PAYE provision.

3. Next steps

- 3.1 The government has today published draft primary legislation for consultation.
- 3.2 HMRC will continue to engage with interested parties, and the comments received will inform the development of regulations and operational guidance, which will be published later in the year.

Annexe A: List of respondents

Deloitte LLP

Grant Thornton UK LLP

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Institute of Chartered Accountants of Scotland

Chartered Institute of Taxation