Independent
Loan Charge
Review

Independent Loan Charge Review:

report on the policy and its implementation

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Contents

Foreword

The progress of the Loan Charge has been unusual. Attracting little attention when first announced, it is now highly controversial with criticism both around its design, and the impact on individuals.

The then Chancellor of the Exchequer asked me to conduct this independent Review in September, addressing whether the Loan Charge is an appropriate response to tax avoidance by individuals who have directly entered into loan schemes; and whether the government's announced changes address the issues that have been raised.

The Review was also asked to take into account the impact on wider taxpayer fairness, and on Her Majesty's Revenue and Customs' (HMRC's) ability to tackle tax avoidance. The Terms of Reference can be found at Annex A.

I have used my discretion in interpreting my remit to come at the main points arising from the controversy, and to cover the necessary context. This report makes recommendations for change as appropriate, covering both the principled challenges to the design of the Loan Charge, and its operation.

The Review has coincided with the final period in which affected users of loan schemes can potentially settle their tax affairs with HMRC ahead of otherwise paying the Loan Charge. I was therefore originally asked to submit this report by mid-November, to enable the government to respond to the Review before the Self Assessment deadline in January 2020. This period was extended as a result of the calling of a General Election, however I hope that the government will still be able to respond promptly ahead of the January deadline.

I am confident that this timetable has not impacted on my conclusions or recommendations, thanks to the published work already available, and the willingness of those who have helped us.

I will describe my method in more detail, but it is right to make clear that I have met a range of individuals impacted by the Loan Charge, along with the Loan Charge Action Group (LCAG), the All-Party Parliamentary Loan Charge Group (Loan Charge APPG), MPs from all the major UK-wide parties, specialist tax advisers, and representative bodies. I also met with HM Treasury (HMT) and HMRC officials, who answered a great number of specific questions.

Most of these groups submitted documents and other evidence, and I met some groups more than once. I also put forth a public request for evidence, and received many valuable contributions including over 700 individual testimonies and impact statements. This, and other material provided by the LCAG and Loan Charge APPG, significantly enhanced my understanding of the relevant issues. While such impact statements cannot be fully representative of the entire population of scheme users, the themes running through them are consistent with the other evidence that I have received. I am very grateful to all those who contributed.

I have also engaged distinguished expert advisers, who have provided invaluable assistance and independent challenge.

Before concluding, I would like to take this opportunity to comment briefly on the nature of the public debate that preceded the Review.

In reading past contributions, the extent to which both sides have become entrenched in their positions was striking. It is unsurprising, but no less disappointing, that this has led to so little proper conversation between the different sides of the debate.

The government would consider themselves to have already made significant concessions during the debate. They are right to flag some of them as potentially having a material impact. Others are less significant. Many of them have been undermined by the perceived difference between a high-level announcement and what actually happens 'on the ground'.

I was expecting that there would be strong views and feelings in this debate. But there were also parts of its nature that I did not expect, or at least hoped not to see. I received evidence of personal targeting of individual tax officials, naming and abusing them, and publishing pictures of their homes and other details. I strongly disapprove of and condemn this type of activity and call on the LCAG and others to do the same.

In the body of the report, I typically use 'we' because I have been supported by a highly efficient team, seconded from HMT and HMRC. I judged that the lead time to set up and inform an external team would involve prohibitive delay, but as mentioned I have secured independent commentary and challenge from a team of professional advisers. I also thank and compliment my team on their work and independent mindedness.

While I have recognised the contributions of others, my conclusions are my own and I hope that my independent Review, and its recommendations, will help to resolve the issues around the Loan Charge.

Sir Amyas Morse

Executive summary

The central questions are whether the Loan Charge is justified in principle and whether its design is proportionate and fair.

Concerns have been raised in two areas. First, whether the Loan Charge deviates too far from the usual operation of the tax system and therefore undermines taxpayers' rights. Second, the distress and hardship amongst those affected. Of particular concern have been the reports of people taking their own lives in cases linked to the Loan Charge, as well as wider impacts on mental health.

I have considered these questions carefully. If asked, 'was some form of policy like the Loan Charge necessary and in the public interest?', I would say 'yes'. It is clear that most people would agree that everyone should pay their fair share of tax. However, the evidence provided to the Review prompts serious questions about how proportionate the Loan Charge was in terms of its design and effect on individuals. The recommendations in this report are designed to address these questions.

While conducting the Review, I frequently spoke to Members of Parliament who told me that they were initially sceptical of concerns being raised by people who were involved in tax avoidance. Such MPs get approached about a huge range of issues and have consistently supported recent measures to combat tax avoidance. . On examining concerns raised by their constituents regarding the Loan Charge, their views had typically evolved. They felt that the Loan Charge raised unique questions, and that their concerns over the proportionality of the Loan Charge should not be seen as wider sympathy for avoiding tax. Instead the questions raised reflect the unique nature of the Loan Charge and their assessment of its impacts. I found this evidence persuasive and my own thinking has progressed along similar lines in light of the evidence that I have received.

There was a need for new policy in 2016. HMRC had had considerable success in getting large corporates to settle after the introduction of new legislation in 2011. However, loan schemes were still used over 10,000 times in 2011-12. This, and subsequent usage, deprived the Exchequer of tax that was clearly due following the new legislation. It was reasonable for the government to act to ensure that this tax was collected.

The Loan Charge therefore emerged in 2016 out of a desire to shut down the use of loan schemes, for reasons of fairness to other taxpayers, as well as value for money, practicality, and to collect revenue for public services.

This followed over 65,000 instances of loan scheme usage from April 2011-March 2016, and a decline in the number of schemes (and taxpayer usage of them) being disclosed to HMRC. In spite of the law being clear, HMRC were therefore not always able to identify the relevant users or efficiently collect the tax that was due. This delay effectively delivered an unjustified advantage to taxpayers participating in loan schemes. Non-disclosure meant that HMRC were unable to use recently established powers – such as Accelerated Payment Notices (APNs) – to collect the tax quickly that was due.

For those reasons, I support the essential purpose of the Loan Charge.

However, the design of the Loan Charge has been described to me by my legal and expert advisers, and the vast majority of contributors, as being highly unusual. Unusual is not always wrong. But it does need to be justified. In my view, elements of the Loan Charge go too far in undermining or overriding taxpayer protections. My recommendations are designed to bring it back in line.

The first point often made by contributors to the Review was how unusual the Loan Charge is in how far it can look back, bringing schemes used since 1999 into scope. Many called this aspect of the design retrospective and unfair.

The justification for looking back to 1999 appears to be that the government always said that the schemes did not work. I found that HMRC did not consistently articulate this to taxpayers before the 2011 legislation, with approximately 40% of the pre-2011 tax years in scope of the Loan Charge not even having had an investigation into them opened by HMRC. Even if HMRC had made their position clearer, taxpayers are entitled to rely on the law as interpreted by the courts – rather than a position taken by HMRC – as the authoritative guide to their tax obligations. At the time of the 2011 legislation being enacted, the courts had not supported HMRC's view about the taxable nature of loan schemes. Indeed, the leading cases from the time had been consistently decided against HMRC's position.

For the twenty year look-back period of the Loan Charge to be proportionate and justified, taxpayers would need to have acted in a way that was perverse in light of a clear legal position. This was not the case. **I therefore conclude that the Loan Charge should not apply to loans entered into by either individuals or employers before 9th December 2010,** being the point at which the law became clear. HMRC should continue being able to settle and investigate cases prior to this point under their normal powers where they have appropriate grounds, and a legal basis, to do so.

My report also makes further recommendations aimed at making the Loan Charge more consistent with other elements of tax policy.

HMRC are bound by strict time limits within which they can investigate tax returns. These give taxpayers certainty over their tax affairs and ensure that HMRC opens investigations in a timely way. The Loan Charge effectively overrides these limits, by treating years in which HMRC opened an investigation (known as Protected Years) in the same fashion as years in which HMRC didn't open an investigation (Unprotected Years).

From December 2010 onwards – when the law about the tax treatment of loan schemes was clear – there is significant evidence that the vast majority of Unprotected Years arose from scheme users not disclosing their loans to HMRC. This evidence is based on HMRC sampling of Unprotected Years within settlements, which I have had independently tested for methodological soundness.

I do not believe that non-compliance, and the failure to make complete tax returns, should be rewarded but I equally do not believe that the usual taxpayer protections should be set aside. **I therefore recommend that taxpayers who made reasonable disclosure of their scheme usage, but for whom the relevant year is unprotected, should not have that Unprotected Year included in the scope of the Loan Charge.** Those taxpayers who did not make reasonable disclosure, and for whom the relevant year is unprotected as a result, should have that Unprotected Year included in the scope of the Loan Charge. From March 2016 onward – when the Loan Charge was announced – HMRC made a reasonable assumption that they need not continue protecting years in which they identified usage of loan schemes. I am therefore also recommending that Unprotected Years from the start of the 2016-17 tax year onwards should continue to automatically be within the scope of the Loan Charge.

A further unusual feature of the Loan Charge is the stacking of years so that income received as loans across multiple years is taxed as if it was all paid in one year. This may have been designed for reasons of practical ease for HMRC, or to incentivise people to settle, but is very different to how income would normally be taxed. I therefore recommend that **affected taxpayers should be able to choose to unstack their outstanding loan balance, and elect to spread their balance over three years**.

I have said that there is a case for the Loan Charge applying from December 2010, but given its abnormal nature there is also a strong case for moderating its impact for those who can afford to pay less. This is particularly relevant as those affected by the Loan Charge are not the 'usual suspects', by which I mean large corporates with an army of advisers, or – for the most part – very rich individuals. Large corporates settled and ceased using schemes when they saw that they were unmistakably not viable after late 2010. Such companies and their employees are therefore not a material element of those subject to the Loan Charge.

The residual group are frequently on mid-range or lower incomes, coming from industries like construction, IT and oil and gas, as well as financial or business services. It is clear to me that many of those affected may not have been fully aware what they were doing when using loan schemes or failed to distinguish between genuine professional advisers and those acting more as salespeople. Certain of them felt that they had little option but to use the schemes.

I have a great deal of sympathy for those people. There is, however, an important principle that the taxpayer is ultimately responsible for ensuring that they have paid the right amount of tax in accordance with the tax laws in force for the relevant period. After careful consideration I agree with the expert testimony given to the Review that any movement away from this principle would be unwise. The enhanced terms that I recommend to ensure that the Loan Charge is affordable for individuals on lower incomes are, however, justified by the fact that such people typically relied upon professional advisers who did not meet expected standards.

A significant proportion of the sums involved can be life-changing. The government has been clear that it does not want to force people into bankruptcy or to sell their main home. I support this view. The mitigations already provided by HMRC, principally in payment terms, are significant, but need to go further, to help achieve those aims and to respond to taxpayer distress.

No individual in scope of the Loan Charge should have to pay more than half of their disposable income in a single year and a reasonable proportion of their liquid assets, and they should not be forced into losing their house or existing pension pot, or being made bankrupt.

My additional recommendations on affordability are deliberately aimed at benefiting those on lower incomes who will pay the Loan Charge, ensuring that they can still draw a line under this experience and move on.

Acknowledging the unusual nature of the Loan Charge and the higher risk that those with less will have to pay for longer, **I recommend that anyone with income of less than £30,000 in the 2017-18 tax year should not have to pay HMRC for longer than 10 years of paying an instalment arrangement and should not pay more than half their disposable income in any given year** (as set out above). This income threshold will affect about 40% of people who used schemes exclusively from 2011 onwards and have not already settled. Any remaining sum should then be written off.

This is a change aimed specifically at those most severely impacted by the Loan Charge, given its abnormal nature. For that reason it should not establish, or be seen as establishing, a wider precedent across the tax system. Indeed, it reflects a reality that in practice HMRC cannot recover money from those who cannot afford to pay.

Some of the specific testimony and evidence I received also suggested a harsher and less edifying picture of the use of the government's powers. While I accept that no one would have had a motivation to contact the Review to tell me about a positive experience, this is not an issue on which a balance of individual experiences is good enough. In interviewing taxpayers and examining detailed impact statements, it became clear that there are significant numbers who feel that they have been badly treated. Examples included tax liabilities from long-dissolved employers arising on individuals when HMRC had never previously opened an investigation, and others who have experienced unacceptable errors and delays in settlement calculations. The evidence I saw supported their viewpoints as being reasonable.

HMRC themselves accept that coordination between the collection branch and other parts of HMRC could be improved, which must mean that it sometimes fails. Evidence received supports the fact that such failures of coordination occur where, for example, someone receives demands for an APN without reference to the state of their negotiations to settle ahead of the Loan Charge. I frequently heard that such failures were particularly difficult for individuals involved, as they created uncertainty over the sums sought by HMRC, and how they could be paid. At times, this created a sense that HMRC was using the Loan Charge as a means to collect settlements that were higher than would otherwise have been the case. These settlements can follow extended discussion between HMRC and the taxpayer, and can be particularly challenging for those less able to access professional advice. While HMRC has a duty to collect revenue, this should always be the right amount of tax – not the maximum that could possibly be collected.

In many of the cases reported, there are connections to the significant increase in HMRC's powers over the last decade to combat tax avoidance. I support the increase in these powers, which are linked to the evolution in public attitudes towards tax avoidance. It is not clear to me, however, that HMRC's accountability or capacity to manage relationships with individual taxpayers have grown to match these powers. **I therefore make recommendations to better match the performance and accountability of HMRC with their increased powers. These are aimed at enhancing trust in HMRC. This is important as it underpins the integrity of our tax collection system and is therefore worth preserving.**

I am also very clear that I have no sympathy for the people who promoted – in some cases pushed – loan schemes after the law became clear. Certain of these salespeople continue to do so, contributing to the large numbers of people who continue to use loan schemes. It is of deep concern that there have been well over 20,000 new usages of loan schemes since the Loan Charge was announced – including 8,000 since the start of the 2019/20 tax year. This reflects the ongoing promotion of these schemes. On no level is that professional behaviour acceptable, and such practices should be stopped.

The proposed legislation extending the reforms of off-payroll working rules (IR35) to primary engagers is also of the first importance in changing the dynamics in this area and will need and deserve support from Parliament.

I thought carefully about the potential effects of my recommendations, in isolation but also when taken together. I would make two overarching comments about how these recommendations interact.

First, I found a number of issues with the Loan Charge, but its overall aim – drawing a line under usage of loan schemes – was justified in 2016 and continues to be so because the schemes continue to be used.

Second, I asked myself 'do my recommendations, by softening some of the effects of the Loan Charge, give the green light to tax avoidance, or weaken HMRC's ability to combat it?' The clear answer is 'no', because – as we have already seen – a key threat to HMRC's ability to combat tax avoidance is the risk of a breakdown in proper co-operation between taxpayers, including those who have taken part in avoidance, and HMRC.

Taxpayer cooperation flows from confidence in fair treatment, and so – in making my recommendations – I have sought to make the Loan Charge proportionate and fair. This means limiting the period over which the Loan Charge looks back to after the law became clear in December 2010; preserving statutory protections around Unprotected Years when a taxpayer disclosed their usage of a loan scheme to HMRC; and recognising the reliance that individuals on lower incomes will likely have placed on professional advice, in ensuring that their payment of the Loan Charge will be affordable.

Ensuring the proportionality and fairness of the Loan Charge also has a wider benefit.

The UK is one of the most tax-compliant countries in the world. HMRC recognises this as a major public benefit, with their policies being generally designed to maintain and enhance the voluntary compliance that sits at the heart of the UK's tax system. The more severe aspects of the Loan Charge – through its reduction in taxpayer protections and the controversy that it has generated – are very different to other anti-avoidance measures, many of which have attracted widespread public and Parliamentary support. If left unchanged, the Loan Charge risks – if not damaging support for such measures – than being unhelpful to HMRC's strategic goal of encouraging voluntary compliance with the tax system.

I have sought to address the concerns raised about the Loan Charge, both from a principled basis and in terms of its impact on individuals.

This does not imply approval of artificial tax schemes, or of tax avoidance. If the Loan Charge controversy shows anything, it shows what a bad idea participating in such schemes was in the past and will be in the future.

My recommendations, if accepted, will bring the Loan Charge back in line with the wider tax system, ensuring that its design is proportionate, and its impacts moderated for those with less.

This should help create a fairer outcome for individuals and the general public, which has been my guiding principle throughout.

Consolidated list of recommendations

The Review has considered the two broad areas of concern: first, questions on whether the Loan Charge is fair in principle and second, distress and hardship among those affected by the Loan Charge. Recommendations are made to address both of these concerns.

The Review also makes recommendations to strengthen HMRC's accountability for how they operate, and to improve future policy aimed at reducing the use of loan schemes. For reasons set out more fully in the report, these recommendations apply in relation to loans entered into by both individuals and employers, unless expressly specified.

Immediate response

1 the government should come forward urgently with a clear timetable for its response to this report and for any necessary legislation to give effect to these recommendations to provide taxpayers with certainty ahead of the 31st January 2020 deadline for assessment to the Loan Charge. This should include appropriate guidance from HMRC to those likely to be affected, and a means of ensuring that taxpayers have time to take appropriate advice before submitting their Self Assessment return or – for those who remain in the settlement process – whether to settle rather than pay the Loan Charge.

2 the Review recommends that HMRC run a settlement opportunity in 2020, to allow any taxpayers outside the scope of the Loan Charge but with a liability arising from loan schemes to settle their tax affairs.

The design of the Loan Charge

The Loan Charge looks back 20 years, establishing a tax charge in relation to behaviour that took place before the relevant law was in effect. This, and other unusual features in its design, go too far and should be changed. The Review recommends the following changes to the design of the Loan Charge:

3 the Loan Charge should not apply to loans entered into before 9th December 2010

4 Unprotected Years arising from loans entered into on or after 9th December 2010, where the relevant taxpayer made reasonable disclosure of their scheme usage to HMRC and HMRC did not open an investigation, should be out of scope of the Loan Charge (subject to recommendation 5 below). Other Unprotected Years should remain in scope of the Loan Charge. This will ensure that taxpayers do not benefit from failing to disclose their tax affairs to HMRC. The approach to defining "reasonable disclosure" should build upon HMRC's ordinary compliance approach in considering the extent to which a Self Assessment return is sufficiently clear about the usage of a loan scheme

5 any Unprotected Years arising from loan schemes entered into during the 2016-17, 2017-18 and 2018-19 tax years should all be included in the scope of the Loan Charge, to ensure that taxpayers who entered into loan schemes after the Loan Charge was announced do not unreasonably

benefit from HMRC having ceased protecting years following the announcement

6 HMRC should refund the Voluntary Restitution elements of settlements made since 2016 that were paid to settle Unprotected Years when the relevant loans were entered into:

a) prior to 9th December 2010; or

b) between 9th December 2010 and the start of the 2016-17 tax year, where the scheme user made reasonable disclosure of their scheme usage in their tax return

7 taxpayers should be entitled to opt to spread their outstanding loan balances over three years, to mitigate the impact of taxpayers paying tax at a higher rate than they ordinarily would. This reduces the effect of stacking their outstanding loan balances into a single year, which artificially created an increased exposure to a higher rate of income tax

8 the extent to which the Loan Charge looks back to activity in earlier tax years dating back to 1999-2000, and the manner in which ongoing interest is charged on payment arrangements has given rise to concerns over how policy on interest is applied within the tax system. The government should review future policy on interest rates within the tax system and report the results to Parliament by 31st July 2020

The individual impact of the Loan Charge

The unusual nature of the Loan Charge can create hardship and life-changing liabilities, particularly if someone has a lower income . For this reason, the Review is recommending that those paying the Loan Charge should experience a significant change from HMRC's usual Time To Pay (TTP) arrangements. These recommendations apply to individuals, including when individuals have employers' Loan Charge liabilities arise on them:

9 all individuals subject to the Loan Charge should only be asked to pay up to half their disposable income each year and a reasonable proportion of their liquid assets. No one should have to sell their primary residence or use their existing pension pot to pay the Loan Charge

10 individuals with income of less than £30,000 in 2017-18 should additionally not have the Loan Charge hanging over their head for any longer than 10 years, and any amount left outstanding after 10 years of paying the Loan Charge should be written off to genuinely draw a line under any outstanding balance. This will allow people to move on after paying what they can afford

11 HMRC should extend to individuals with income from £30,000 up to £50,000 in 2017-18 the same payment terms that were offered to such individuals who settled their tax affairs rather than pay the Loan Charge. Such individuals should be automatically able to pay the Loan Charge over up to five years without having to provide HMRC with further details of their asset ownership

HMRC implementation

HMRC's performance does not always live up to the standards they set themselves. Given their significant and justified powers, it is even more important that there are high levels of accountability. Trust in HMRC is an important part of the integrity of our tax collection system and is worth protecting. To strengthen this the Review recommends that HMRC should:

12 fund an external body to provide independent advice to lower income taxpayers who are discussing payment arrangements and debt collection with HMRC, including on potential suitability of an individual voluntary arrangement (IVA) or other arrangements

13 update taxpayers at least annually about the status of open tax enquiries and, where they do not do so, have this non-communication taken into account by the First-tier Tribunal (FTT) if a taxpayer applies to have an open enquiry closed

14 report to Parliament on its implementation of the Loan Charge before the end of 2020, drawing on input from their recently established Customer Experience Committee, representative bodies, charities focused on lower income individuals, and other professionals. This report should also address common themes arising from other recent reports, including from the House of Lords Economic Affairs Committee (EAC) and the Adjudicator

15 review its Charter to set higher expectations of performance during interactions with members of the public, and to ensure that staff are trained to meet these expectations

Next steps and the future

The Loan Charge is a one-off with no prospective effect. The factors which led the government to tackle the use of loan schemes remain, including significant usage of schemes. Evidence shows that usage of loan schemes continues, with there being more first-time users in 2017-18 (over 6,000) than in any year dating back to 1998-99. To address this, and wider issues that have been raised during the Review, we are recommending the following:

16 given the one-off nature of the Loan Charge, government should explain how it will tackle loan scheme usage in the future

17 the government must improve the market in tax advice and tackle the people who continue to promote the use of loan schemes, including by clarifying how taxpayers can challenge promoters and advisers that may be misselling loan schemes. There should be a new strategy published within 6 months, addressing how the government will establish a more effective system of oversight, which may include formal regulation, for tax advisers

18 the strategy for communicating what is considered tax avoidance must be improved to reflect the 'mass market' nature of loan schemes. In particular, HMRC should continue enhancing its usage of Pay As You Earn (PAYE) Real Time Information to communicate with taxpayers who they suspect may be engaging in tax avoidance, and proactively put taxpayers directly on notice of its view

19 that future published government impact notes of tax changes should take proper account of the direct impact on the affected population. These assessments should also explicitly include interactions between different taxes

20 that, as campaigns on taxpayer issues such as the Loan Charge are likely to be a feature of debates in tax policy in future, HMRC should learn from the Loan Charge to better respond to such campaigns and communicate more effectively

Section A: Context and history of the last 20 years

The Loan Charge does not stand alone, and nor do the practices that it tried to tackle.

Understanding some of the most important questions underpinning the review, including whether the Loan Charge was an appropriate response to those practices, therefore requires an understanding of a wider set of issues beyond those strictly labelled as the Loan Charge.

These include what government actions preceded it over the last 20 years, what drove the behaviours it was designed to shut down, and the point at which the taxable nature of loan schemes became clear.

The next two chapters set out the broader context, summarise the emergence of loan schemes, and how successive governments and the legal system responded.

Chapter 1

1999 to 2010 and the development of loan schemes

1.1 This chapter starts to answer some of the wider questions underpinning the Review by setting out the context of changes in the labour market, public opinion on tax avoidance, and the response of different governments to the emerging market in loan schemes up until 2010.

The labour market has evolved in recent decades

1.2 It is, of course, nothing new for employers to try to decrease their employment costs, including by straying into tax avoidance. In the early 1990s, for example, employment tax avoidance schemes paid employees' salaries and bonuses using assets like gold bullion, Persian rugs, rapidly depreciating currencies, and platinum sponges before such schemes were targeted by legislation.

1.3 What has changed in a number of industries is the trend towards self-employment and different ways of working since the mid-'90s. Full time work continues to make up the majority of employment in the UK, but levels of self-employment have increased substantially from 12% of the labour force in 2001 to 15% in 2017.[1]

1.4 This change is significant for two reasons.

1.5 First, as the Taylor Review noted, these changes can in some instances create an imbalance of power between employers and individuals. The flexibility of working arrangements has many benefits but can also give the primary engager, agencies, and others considerable power to dictate the employment terms that individuals should use.[2]

1.6 Second, it was only possible for loan schemes to proliferate due to the creation of a market of potential individual scheme users.

The tax rules for contractors have also changed

1.7 Changes in tax rules and shifts in labour markets have affected the employment status of individuals seeking, or being asked to enter into, self-employment.

1.8 The government introduced legislation in 2000, known as IR35, to counteract the use of Personal Service Companies (PSCs) as a method of 'disguising employment'. These off-payroll working rules sought to ensure

1 'Trends in self-employment in the UK', Office of National Statistics, 2018

2 'Good work: the Taylor review of modern working practices', Matthew Taylor, Greg Marsh, Diane Nicol, and Paul Broadbent, 2017

that those using PSCs to disguise their employment status were charged tax on the underlying employment relationship.

1.9 The Review heard that this increased uncertainty for workers, with it being said that individual workers often would struggle to know whether they were in scope of the legislation. Individuals therefore looked for ways to retain their level of pay after tax, but without the risk associated with working through a PSC.

1.10 One option was to work through an umbrella company – a structure which provides employment to a number of individuals, signing contracts to provide individuals' labour to third parties. This is and was always possible without entering into a loan scheme, with the vast majority of people employed through umbrella companies not using a scheme. Neither was scheme usage widespread amongst freelancers; of a population of 2 million HMRC estimate that just 2.5% used loan schemes.[3]

1.11 But those who devised loan schemes now had a larger market of potential users, such as those attracted to arrangements which would provide certainty on IR35, or an increase in take home pay compared to alternative options. The Review also saw evidence of loan schemes being sold as part of a package alongside employment through umbrella companies, merging two distinct concepts.

1.12 The original IR35 proposals would have put the responsibility on primary engagers to assess whether any of their relationships with contractors' PSCs meant that IR35 applied. This would have placed a much stronger accountability on the primary engagers making the contracting decisions, a principle that this Review supports.

1.13 It is therefore unfortunate that, following concerns being raised by business, these responsibilities were instead placed on PSCs, and effectively individual workers, as a result. This meant that contractors were required to assess whether they were within the scope of IR35, and to assess their tax liabilities on this basis.

1.14 It is important to note that, in an initiative which this Review supports, the government announced in 2018 that it would put responsibility for operating IR35 onto large primary engagers in the private sector from 2020, having already done so in 2017 for public sector engagers.

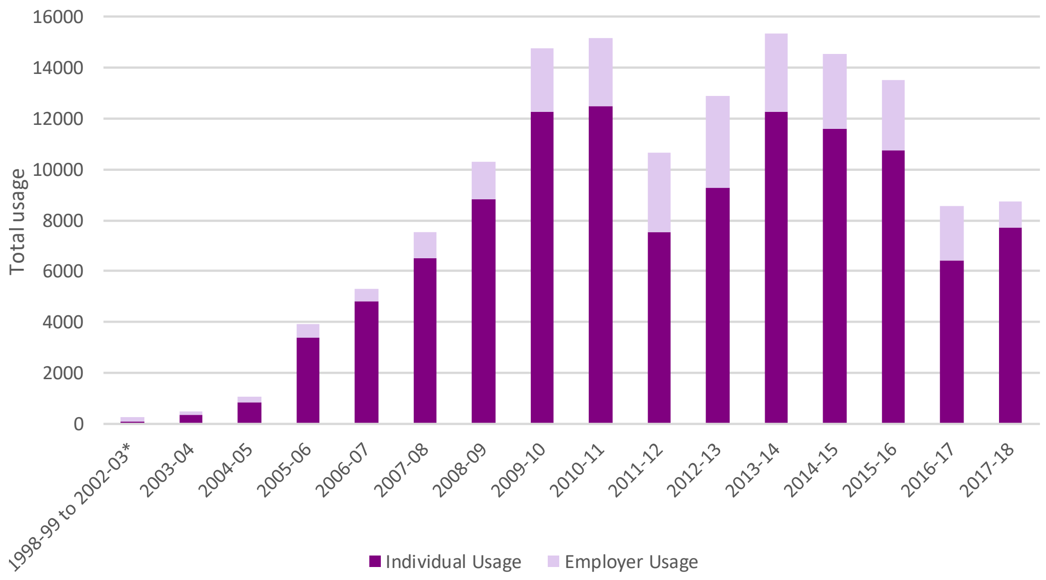
1.15 **The Review therefore supports moves to make primary engagers more responsible for the tax status of those they effectively employ**

1999 to 2004: HMRC starts to respond to the rise in loan schemes

1.16 With an expanding market of interested individuals, scheme use started to grow from a low base during the early 2000s, moving from being used almost exclusively by large employers to becoming more of a mass market product.

3 'Section 95 of the Finance Act 2019: report on time limits and the charge on disguised remuneration loans', HM Treasury, 2019

Chart 1.A: Number of loan schemes used each year



Source: HMRC response to request from Review.[a]

a All numbers in the data provided were rounded to the nearest 10, except for between 1998-1999 and 2002-2003. The figure for that period is a range of between 60 and 70, though we represent it as 70 on the graph.

1.17 HMRC had begun to challenge the use of loan schemes, focusing largely on tax professionals and large corporate employers who were driving most usage of loan schemes and would have yielded greater amounts from settlements. Arguably taxpayers may not have been aware of this approach, and therefore not appreciated HMRC's position on schemes. The investigation of schemes in the early 2000s was generally focussed on the employer, typically advised by a promoter. The evidence from HMRC is that they would usually only contact scheme users' promoters or agents, not generally individuals. In many cases, scheme users are therefore unlikely to have understood HMRC's position in this period, or have had it brought to their attention.

1.18 HMRC's position at the time was also not supported in the courts. In 2002's *Dextra Accessories v HMRC*, the Special Commissioners found that the employee benefit trust (EBT) scheme under consideration achieved the "outcome promised when they were being marketed".[4] While HMRC was eventually successful in appealing narrower arguments around corporation tax in the House of Lords the question around whether the loans were income was not considered further. It took until 2017 – subsequent to the

4 *Dextra Accessories Ltd & Ors v Inspector of Taxes* [2002] STC (SCD) 413

announcement of the Loan Charge – for *Dextra* to be overruled by the Supreme Court, which concluded that it had been wrongly decided.[5]

1.19 While loan scheme use was growing in the early 2000s, HMRC had not yet received judicial support that loan schemes did not work, and that loans should be taxed as income. Taxpayers did not, therefore, have to accept HMRC's view. Evidence received by the Review consistently supported the view that such schemes were not seen as being aggressive tax avoidance at the time.

2004 to 2010: increased loan scheme usage by individuals and HMRC's response

1.20 The use of loan schemes by large employers continued between 2004 and 2010. But, significantly, simpler versions were now also increasingly being used by owner-managed businesses (OMBs) and individuals providing services through a PSC. The market in loan schemes was therefore changing.

1.21 Evidence from HMRC to the Review set out that such OMBs and individuals were typically introduced to loan schemes by their professional advisers, or by an enabler selling the scheme on behalf of a promoter. For both individuals and employers during this period, HMRC continued to typically only contact scheme users' promoters or agents, rather than the individuals with whom tax liability ultimately rested.

1.22 There was already a long established regime for taxing the benefits of loans to employees. Employees who receive interest free loans or loans at a rate of interest below a prescribed official rate have to pay tax on the benefit they receive.

1.23 Many scheme users were therefore declaring loans on their tax returns and paying tax on the benefit received in accordance with these beneficial loan rules, without any challenge from HMRC. This might have been because the source of the loans was not obvious, but nevertheless it was another indication to scheme users that receiving loans was an acceptable form of tax planning. The Review heard repeatedly from people affected by the Loan Charge that they disclosed their loans to HMRC, including through the Disclosure of Tax Avoidance Schemes (DOTAS) regime introduced in 2004, and assumed that the lack of subsequent challenge meant that HMRC were content with the arrangements.

1.24 HMRC's strategy did, however, begin to change presumably in reaction to the rising number of users and tax at risk. A public statement about employment income related tax avoidance was made in a written ministerial statement in 2004.[6] This high-level announcement set out that the government would close down employment related tax avoidance arrangements, and would legislate to ensure the proper amounts of income tax and National Insurance contributions (NICs) are paid on remuneration from employment. It did not specifically mention loan schemes.

5 *Inspector of Taxes v Dextra Accessories Ltd & Ors* [2005] UKHL 47

6 'Written Ministerial Statement: 2nd December 2004', The Paymaster General, 2004, Column 46WS

1.25 From 2009 onwards, HMRC also published its view in specialist Spotlight articles, which reach a limited number of agents and tax professionals. Evidence about the readership of relevant Spotlights from the time is not available, but in 2015 (when data is available) the four articles published to that point received an average of just 520 views each. The Review therefore concludes that both individual scheme users, and those using schemes through their employers, would likely have continued to be largely unaware of HMRC's position at this time.

1.26 The legal position at the time also remained unclear, with the courts not accepting HMRC's view of the tax consequences of loan schemes. The 2008 decision in *Sempra Metals v HMRC* rejected the government's arguments that loans made by an employer's EBT were subject to income tax.[7]The case was not appealed to the higher courts, which may have given scheme users at the time a degree of comfort that the legal position was settled. As had been the case with *Dextra*, it would take until 2017 for the Supreme Court to conclude that *Sempra* had been wrongly decided

1.27 Overall, this period saw the continued use of loan schemes by large employers, while they began to be used by OMBs. Most significantly it saw proliferation of loan scheme use by individuals, leading to a different type of market and different challenges for HMRC:

- the decisions of tribunals in this period were that loan arrangements achieved their intended purpose, and that HMRC's view of the law was incorrect

- the absence of court or tribunal support for HMRC's position that the schemes did not have the effect intended meant that taxpayers could reasonably conclude that scheme usage worked

- HMRC's focus on communicating with advisers and tax professionals, as opposed to scheme users, about investigations into their tax affairs during this period meant that scheme users would frequently not have been aware of HMRC's position even when investigations were opened

- approximately 40% of tax years in this period within which loan schemes were used (and are in scope of the of the Loan Charge) did not have an investigation opened into them by HMRC, meaning that the relevant taxpayer would not have been notified of HMRC's interest in their tax affairs

- the growth of different ways of working in the wider labour market, and the reaction to IR35, created a larger population of potential scheme users

7 *Sempra Metals Ltd v Revenue and Customs Commissioners* [2008] STC (SCD) 1062

Chapter 2

2010 to the Loan Charge

2.1 The continued growth in the use of loan schemes, a shift in public attitudes, and the changing population of users led to the government taking much more significant action from early 2010 to 2016. This chapter summarises government action and litigation during this period.

2.2 This included introducing legislation targeted specifically at arrangements such as loan schemes which had the effect of creating a much clearer legal position on their use.

2.3 The result was a consistent view from our expert advisers, outside experts, and many others to whom the Review spoke that the 2011 legislation marked a significant change in the landscape for these types of schemes.

Shift in public attitudes to tax avoidance

2.4 Public support for tackling tax avoidance seemingly increased after the financial crisis in 2008, and Parliament responded by giving HMRC increased powers to tackle this behaviour. Details of certain of these powers, most of which have been supported in Parliament on a cross-party basis, are set out below.

Table 2.A: Increased HMRC powers

No.	Power	Legislated for	Purpose
1	Naming of deliberate tax defaulters	2009	To publish the names of tax defaulters who have made deliberate errors in their tax returns or deliberately failed to comply with tax obligations
2	General Anti-Abuse Rule (GAAR)	2013	To deter taxpayers from entering into abusive tax arrangements, and to deter would-be promoters from promoting such arrangements
3	Accelerated Payment Notices (APNs)	2014	To oblige a taxpayer who has used a tax avoidance scheme to, if certain conditions are met, pay the disputed tax within 90 days of the APN being issued
4	Follower Notices	2014	To oblige a taxpayer who has used a tax avoidance scheme of a type shown in litigation to be ineffective to settle their dispute or otherwise face a financial penalty

5	Promoters of Tax Avoidance Schemes (POTAS) rules	2014	To require monitored promoters of tax avoidance schemes to disclose details of their products and clients to HMRC, and minimise the risk of tax loss via avoidance schemes
6	Requirement to Correct (RTC)	2017	To require taxpayers with undeclared offshore tax liabilities to disclose these to HMRC, to enable HMRC to take appropriate action in response
7	Penalties for enablers of tax avoidance	2017	To impose penalties upon enablers of tax avoidance schemes that are subsequently defeated by HMRC

2.5 Some witnesses looked back approvingly to times before those powers, when HMRC and tax advisers and their clients conducted prolonged battles through the courts, contesting cases on a more or less even basis and delaying resolution for long stretches of time. The Review does not agree with this perspective. From the point of view of the average UK citizen, there is a need to collect revenue for the country's public services in an efficient manner. **The Review is therefore explicit that it supports the general direction of travel in ensuring the government has greater powers to tackle tax avoidance**. References in the Review to HMRC's increased powers should be read as referring to powers of the type set out above.

2010 marked a significant increase in action against loan schemes

2.6 From early 2010, it was clear that the government would legislate to ensure that loan schemes did not avoid income tax and NICs.

- March 2010: the then Labour government said at the Budget that it would tackle the schemes, including through introducing new legislation
- June 2010: this was repeated by the coalition government in their June Budget
- 9th December 2010: draft legislation was published for consultation alongside a written ministerial statement
- 19th July 2011: the legislation, which had been amended following consultation, received Royal Assent

Box 2.6 A: The 2011 legislation and its December 2010 start date

In 2011, new legislation was inserted into the Income Tax (Earnings and Pensions) Act 2003. This new section is often referred to as Part 7A.

It charged income tax and NICs on the full value of a loan made to an employee (or related party) from a third party, such as a trust.

In contrast to the Loan Charge, which applies to loans made up to 20 years ago, the 2011 legislation applied from the start of the 2011-12 tax year.

Anti-forestalling rules were also included to ensure that taxpayers did not enter into schemes prior to the start of the 2011-12 tax year in order to get around the requirements of the new legislation. These covered certain transactions from 9th December 2010 onwards: the date when the legislation was published in draft and a written ministerial statement was made in Parliament.

Part 7A became law as part of the Finance Act 2011.

2.7 Expert commentary at the time sets out that, while the legislation was not perfectly drafted, it was understood as ensuring that income provided to employees through schemes using third parties, such as loan schemes, was subject to income tax and NICs.

2.8 Professional advisers discussing the legislation concluded that it was taking "a double-barrelled approach of very general provisions" alongside "quite specific provisions to target certain schemes in existence."[1]

2.9 PricewaterhouseCoopers noted that, "PAYE and NICs will be due when a third party lends money from 9th December unless it falls within one of the very limited exemptions".[2] Guidance published by LexisNexis was similarly clear about the purpose of the legislation, "the disguised remuneration (DR) legislation introduced in the Finance Act 2011 was a warning to employers and promoters of tax avoidance schemes that the use of EBTs and other contrived remuneration structures to avoid, defer or reduce income tax liabilities would be strongly challenged."[3]

2.10 The evidence provided to the Review by tax experts considered the 2011 legislation to be a "dramatic change" in the law covering loan schemes and that there was a clear distinction between the arrangements put in place before and after its introduction. It was commonly referred to as 'keep off the grass' legislation, meaning it is wide in scope to ensure that the government's intention is clear and can be used to challenge a number of variants.

2.11 The 2011 legislation had a significant impact on the nature of loan schemes, with loan schemes of the type that existed prior to the legislation no longer delivering tax benefits. This led to loan schemes becoming increasingly contrived to seek to get around the requirements of the 2011 legislation. Five separate GAAR Advisory Panel decisions (all from 2018 but relating entirely to loans entered into from 2011 onwards) show that such contrived

1 'Disguised remuneration: ITEPA part 7A an introduction', Harriet Brown. Tax Chambers, 15 Old Square, 2011

2 'More certainty on pensions and disguised remuneration', PricewaterhouseCoopers, 2011

3 'Disguised remuneration – overview', Tolley and Karen Cooper, CooperCavendish LLP, 2011

schemes are not reasonable courses of action in relation to the relevant law.[4] These decisions have arisen both from employers establishing employer financed retirement benefit schemes (EFRBs), and schemes aimed at benefiting contractors who had previously been employed through a PSC.

2.12 These new rules left open the tax situation for loans made to employees prior to 9th December 2010. Published HMRC guidance made it clear that such loans were not caught by the new rules but that HMRC would continue to challenge "some types of transactions" under previously existing law, including in litigation.

Behaviour did change after the 2011 legislation, though this impact was not sustained

2.13 After the introduction of the legislation, larger employers were far less likely to enter into loan schemes and HMRC focussed its resources on encouraging those who used schemes before 2011 to settle. The EBT Settlement Opportunity (EBTSO) was successful in ensuring a significant proportion of large employers settled their pre-2011 use of schemes.

Box 2.B: EBT Settlement Opportunity (EBTSO)

This opportunity was available to employers, notably large corporates, who used schemes before 2011.

Employers could settle by paying income tax, NICs, late payment interest, and inheritance tax. Payment ensured that they did not face a charge on the money or assets held by a trust or any investment growth.

If HMRC had not yet protected a year, then the employer could choose to pay voluntary restitution to ensure a future charge did not arise.

HMRC wrote to over 5,000 employers to let them know about the EBTSO. In total, approximately 700 settled under EBTSO, raising around £1.6 billion.

2.14 This is an example of a settlement process working as it should. **No part of this report should be taken as support for reopening the associated cases, or those settled prior to March 2016**. HMRC's evidence to the Review was clear that large corporate employers and their employees do not form a material part of the population within scope of the Loan Charge as a result of these successes. The Review notes that the withdrawal of large corporates from schemes at this point is likely to reflect the quality of professional advice available to such employers, relative to that available to the smaller employers and individuals who continued using schemes after 2011.

4 GAAR Advisory Panel decisions are available online, dated 26th January; 28th February; 25th June; 11th October; and 12th October 2018

Some people continued to enter loan schemes after Finance Act 2011

2.15 HMRC were clearly successful in ensuring larger employers no longer used loan schemes, and settled their pre-2011 use, thanks to the introduction of the legislation and employer settlement opportunities.

2.16 However, this success was not matched with individuals. Only a limited number of those who had used the schemes before 2011 settled. Despite a 40% decrease in individual usage in 2011-12, the number of individual scheme users had returned to its previous levels three years later.[5]

2.17 This was despite the fact that the government had done more to try to raise awareness and had started to have more success in the courts.[6]

2.18 HMRC lost their challenge against the use of a loan scheme by an employer, Rangers Football Club, between 2001 to 2009 at the FTT and Upper Tribunal (UT) in 2012 and 2014 respectively. This is referred to throughout this report as *Rangers*.[7]

2.19 However, they had a success in *Boyle v HMRC*, a case which relates directly to individual scheme users.[8] Decided by the FTT in 2013 it relates to an early loan scheme, known as Sandfield. In that case loans entered into between 2001 to 2004 were made in Romanian, Belorussian and Uzbekistani currencies at an artificially high rate of depreciation so that any repayments would have been of economically negligible value. The Tribunal held that the loans were not genuine and were subject to income tax.

2.20 Following this judgment HMRC launched a settlement opportunity focussed on individual scheme users.

Box 2.C: Contractor Loan Settlement Opportunity (CLSO 1): July 2014 and September 2015

This opportunity to settle with HMRC was available to individuals who used a loan scheme up to 5th April 2011, where there was an offshore employer.

They could settle by paying income tax on the loans they received in years where HMRC had an open Enquiry or valid assessment. This settled all years, including where HMRC did not have an open Enquiry or valid assessment.

HMRC wrote to around 11,000 known users at the time, as well as their agents.

5 Data from HMRC response to request from the Review

6 In addition to the Budget announcements, the government had published further Spotlight articles online, though as noted these are targeted at a professional population and typically have a small readership.

7 *Murray Group Holdings Ltd v Revenue and Customs Commissioners* (2012) UKFTT 692 (TC); [2013] S.F.T.D. 149 (FTT (Tax)); *Murray Group Holdings Ltd v Revenue and Customs Commissioners* (2014) UKUT 292 (TCC); [2015], S.T.C. 1 (UT (Tax))

8 *Boyle v HMRC* [2013] UKFTT 723 (TC)

Around 1,500 individuals settled under CLSO 1, bringing in around £31 million. The average settlement was around £19,800 and most agreed payment arrangements of less than 2 years.

2.21 Although only a low proportion of those contacted under CLSO 1 elected to settle their tax affairs, the Review does not think that solely arose from a lack of motivation to settle. The particularly contrived nature of the loans in *Boyle* means that it is not commonly viewed as the leading case in relation to the tax treatment of loan schemes, which is seen as the *Rangers* case. HMRC had been defeated in court in both 2012 (at the FTT) and 2014 (at the UT). Although the judiciary's view of the tax treatment of loan schemes was evolving by 2014, it was not yet clearly in support of HMRC's arguments.

2.22 HMRC began to have success in their appeal in 2015 against the earlier decisions in favour of Rangers Football Club. The Inner House of the Court of Session (equivalent to the English Court of Appeal) found in HMRC's favour in 2015. The case was finally decided in HMRC's favour by the Supreme Court in 2017.[9] The decision held unanimously that the contributions into the trust were employment income, with a PAYE liability for both income tax and NICs falling on the employer. This followed a change in HMRC's argument at the Court of Session, that PAYE was due upon payments by the employer into an EBT – meaning that the circumstances in which the tax liability could be transferred from the employer to individua scheme users was narrower than under HMRC's previous argument which had not been accepted by the FTT or UT. The Supreme Court also held that two earlier cases (*Dextra* and *Sempra*), had been wrongly decided by the lower tribunals.

2.23 There are a number of reasons why individual usage of loan schemes may have started to rise again during this period, despite the 2011 legislation and other factors mentioned above.

2.24 Schemes evolved that purported to get around the legislative requirements. These became increasingly convoluted, including those that attempted to obscure the loan elements of the arrangements, and self-employed schemes that did not involve an employer entity.

2.25 Testimony provided to the Review also stated that significant numbers of individuals may not have understood the legal position at the time, including because of advice given out by promoters and professional advisers.

2.26 Despite the mass market nature of the scheme usage, HMRC's communications until 2014 continued to be aimed at tax professionals through the technical Spotlight articles.

2.27 HMRC's compliance focus also continued to be on a limited number of individuals, working their cases with a view to litigating them and achieving a decision which could be applied to similar schemes and a wider number of cases. Therefore, during this period HMRC continued to have limited contact with individual scheme users, relying instead on communicating with their promoter or agent who would agree to keep their clients informed of

9 *RFC 2012 Plc (formerly The Rangers Football Club Plc) v Advocate General for Scotland* [2017] UKSC 45.

progress. This was the case even for scheme users from the early 1990s and 2000s, where many perceived that their affairs were resolved having not heard from HMRC for a long period.

2.28 From 2014 onwards (and as discussed more fully later in this report), HMRC moved away from this approach towards communicating more directly with scheme users. This approach continues to be developed, making use of Real Time Information that is now accessible to HMRC which can indicate whether an individual is participating in a loan scheme.

Changes in professional standards

2.29 As government action, and public views as to what is acceptable tax planning, have shifted so too have professional standards. What might once have been considered acceptable tax planning is now seen as unacceptable tax avoidance.

2.30 As an example, professional guidance used by one representative body was changed from 2017 to be clear that "Members must not create, encourage or promote tax planning arrangements or structures that (i) set out to achieve results that are contrary to the clear intention of Parliament in enacting relevant legislation and/or (ii) are highly artificial or highly contrived and seek to exploit shortcomings within the relevant legislation".[10] Previously, it was left to members of representative bodies to decide what was or was not tax avoidance, taking into account HMRC's views and the GAAR.

2.31 This reflects a welcome move and improvement in the tax advisory profession. Unfortunately, there remains a market of unscrupulous tax advisers, including those who continue to promote loan schemes. The Review goes on to make recommendations to tackle their practices

Conclusion

2.32 There were clear reasons why the government felt it should look again at the use of loan schemes in 2016:

- usage might have peaked, but there were still almost 11,000 uses by individuals in 2015-16, with over £100m due in tax as a result[11]
- there was a large number of people under investigation who had used the schemes, but had not settled[12]
- the experience from the legal cases, including but not limited to *Rangers*, was that pursuing those who had used the loan schemes could be time consuming and challenging

10 'Professional Conduct in Relation to Taxation', Chartered Institute of Taxation, 2017

11 Data from HMRC response to request from the Review

12 The government estimates that some 50,000 people are subject to the Loan Charge, meaning that they used a loan scheme between 1999 and 2019 and have not settled with HMRC before March 2016. This figure is disputed by certain critics of the Loan Charge.

2.33 There were legitimate reasons therefore for the government to consider whether a new strategy, including further powers, was needed.

2.34 However, there are significant questions regarding whether the strategy of the Loan Charge, and its specific design and implementation, was a proportionate solution to the problem. That is what this Review has considered and makes recommendations to address.

Section B: Design of the Loan Charge

The government's stated policy objective at Budget 2016 was to shut down the use of loan schemes.

In designing the Loan Charge, it was given considerable power to do so, as the policy was purposefully planned in such a way that taxpayers facing it either have to settle, pay off the outstanding loan balance, or pay the Charge.

The Review supports the government's ultimate objectives for the policy. However, as this section of the report sets out, the design of the Loan Charge is highly unusual. While unusual policy design is not inherently wrong, it creates an obligation to ensure that all elements of the policy are justified and proportionate. That was not the case for the Loan Charge.

The next section summarises the unusual design, before the ability to look back 20 years is considered in more detail.

Key recommendations in this section:

- the Loan Charge should not apply to loans entered into before 9th December 2010

- for loans entered into on or after 9th December 2010, Unprotected Years should remain in scope of the Loan Charge unless the relevant taxpayer made reasonable disclosure of their scheme usage to HMRC in relation to that year

- taxpayers should be entitled to opt to spread their outstanding loan balances over three years, to mitigate the impact of taxpayers paying tax at a higher rate than they ordinarily would

Chapter 3

The objectives and unusual design of the Loan Charge

3.1 The government's intention with the Loan Charge was to tackle both the historic and continued use of loan schemes.[1]

3.2 The Review supports the government's ultimate objectives in designing the policy specifically to stop future tax avoidance through loan schemes, reduce the need to fight multiple cases in the courts, and to accelerate the collection of tax due. The Review also supports the basic intent behind the Loan Charge, as it is appropriate for HMRC to be at an advantage - and to make use of increased powers – when acting against tax avoidance.

3.3 The Loan Charge gives HMRC a powerful tool to ensure that affected taxpayers can either settle their underlying tax liability, or otherwise pay the Loan Charge. HMRC has recently noted, however, that "the number of settlements is lower than we would have liked".[2] Based on the figures that HMRC have provided to the Review, under a third of the approximately 10,000 employers and 50,000 individuals they estimate are affected have provided the necessary information to settle. Of those, approximately 3,200 employers and 4,800 individuals have settled. A maximum of one third of the affected population will therefore be able to settle, and it remains possible that over 85% of the population that HMRC estimate to be affected will face the Loan Charge.[3]

3.4 It is noteworthy that so many people may pay the Loan Charge rather than settle, given HMRC's guidance that settling was likely to be more beneficial than paying the Loan Charge. It is likely that this relates to the affordability of settling underlying liabilities and the Loan Charge itself, which is discussed in Chapter 7 of this report.

3.5 The Loan Charge, alongside other changes, has also not been successful in stopping use of the schemes. HMRC reported to the Review that over 6,000 individuals entered into loan schemes for the first time in 2017-18, and 8,000 individuals have entered into loan schemes since April 2019, of whom 3,000 are first-time users.[4]

1 Paragraph 1.217, Budget 2016

2 'Oral evidence: HMRC Standard Report 2018-19, HC 28', House of Commons: Public Accounts Committee, 2019

3 Data from HMRC response to request from the Review

4 Data from HMRC response to request from the Review

The design of the Loan Charge

3.6 The overall design of the Loan Charge has been described by the Review's external advisers and the vast majority of expert contributors as being highly unusual and needing further scrutiny.

3.7 The following features, both of the Loan Charge itself and settlement terms published in 2017 before it applied, were particularly highlighted.

The Loan Charge

3.8 **The Loan Charge can look back 20 years.** It applies to loans made between 1999 to 2019 and which were not been paid back by 5th April 2019. This design has been described by HMT as 'retroactive'.[5] It has also commonly been called 'retrospective' by critics, who point out the loans were made in the past, and that HMRC did not act at the time. This report refers to it as 'looking back'. The Review's legal advisers found that there was no precedent for that element of the design.

3.9 The Review heard many concerns about this ability to look back 20 years and found no articulated rationale by the government for choosing 1999.

3.10 **The Loan Charge stacks loans made into a single tax year.** It imposes a tax charge in a single year on a stack of all outstanding loans, regardless of the number of years over which these loans were entered. An intention behind this element of the design was to encourage taxpayers to settle rather than pay the Loan Charge. The effect of the income stacking can be to bring the outstanding loans into a higher tax band than would have been the case had they been taxed at the point at which they were entered into.

3.11 **The Loan Charge permits more straightforward transfers of liabilities.** HMRC has existing powers to transfer liabilities of certain tax debts from employers to owner/managers of the employer. Employers' Loan Charge liabilities are capable of arising on individuals (typically the owner/managers of the employer but, in certain circumstances, employees) in a way that goes beyond other elements of the tax system which permit transfers of liabilities in more limited circumstances. The Review received particular evidence regarding employers' liabilities arising on individuals when the employer had been dissolved many years ago, particularly when no investigation into the employer's tax affairs had been opened at the time (and so arose from an Unprotected Year).

The 2017 settlement terms

3.12 **Settlements require Voluntary Restitution from those who wish to settle Unprotected Years ahead of the Loan Charge**, even though HMRC would not otherwise be in a position to collect tax on those years. This is the only way that scheme users can ensure that they will not face the Loan Charge in relation to Unprotected Years.

3.13 **Settlements include interest, often charged over a long time period on Protected Years.** Interest on Protected Years is applied at a statutory rate set by government, currently 3.25%, from the point at which the tax is deemed due. Although this interest rate is consistent with other areas of the tax system, it can apply in this instance from up to 20 years ago, running until the date that the settlement is agreed.

5 'Uncorrected oral evidence: The Financial Secretary to the Treasury', Select Committee on Economic Affairs, 2019

A further 1% is then added to the rate of interest for the duration of any payment arrangement, to reflect the risk to HMRC of entering into a payment arrangement.

3.14 For the Loan Charge, by contrast, interest is charged at 3.25% from the date the Loan Charge is due. This is 31st January 2020 in most cases, running until the point at which the Charge is paid off.

3.15 The length of look back means that the interest rates have a disproportionately significant effect: for example, using a rate of 3.25% compounded over 20 years would double the amount owed. The effect of this has been exacerbated by HMRC's historic approach of not communicating directly with scheme users, meaning that in some cases interest has been accruing without scheme users being aware that HMRC have an investigation open.

The effects of the unusual design

3.16 Whilst the impact of the Loan Charge does not result from just one feature, the Review noted that looking back 20 years contributed to at least two of the areas particularly impacting on taxpayers as reported to the Review in individual testimony.

Affordability

3.17 The Loan Charge impacts a large number of people and many will be asked to pay significant amounts. Of settlements entered into through June 2019, the average (median) is approximately £18,000, with HMRC anticipating that it will typically be financially more beneficial for scheme users to settle rather than pay the Loan Charge.[6] The mean amount for settlements entered into until June 2019 is significantly higher, at £59,000.

3.18 The Loan Charge coming due therefore has the potential to require a life-changing sum of money from a significant proportion of those required to pay. Broadly, this situation resulted from one or more of the following:

- the Loan Charge looking back over a long period, so scheme users' circumstances will have changed considerably since they entered into schemes
- many scheme users reporting that the lack of visible challenge by HMRC had led them to continue using schemes for multiple years
- the difference between what was paid in tax and what would have been owed if the tax had been sought by HMRC at the time and paid in a more typical fashion
- and the widespread, mass market, use of the schemes over the past two decades, accounting for why such a large number of people are affected

3.19 This issue is covered in further detail in Chapter 7 of this report.

6 HMRC analysis provided to the Review following a request.

Unexpected

3.20 Many of the impact statements we received said that the scheme users were not expecting to be asked to pay this tax. Factors that influenced this included:

- limited communications from HMRC about the status of their case, particularly before HMRC's case strategy changed in 2014. In many cases a long time passed since the loans were made so people expected the issue to have been closed or to have been notified by HMRC earlier if there was an investigation into their tax affairs. HMRC did not open an investigation into the scheme usage of approximately 40% of pre-December 2010 scheme users, and so people in this category may, in particular, not have been aware of HMRC's position until the Loan Charge was introduced

- scheme users often trusted the advice from their accountants, those promoting the schemes, and other tax or legal professionals which stated that they would not have to pay tax on the loans. Promoters sometimes misrepresented to scheme users the nature of declarations to HMRC under the DOTAS system, so that they were seen by users as a kite mark, constituting approval by HMRC

3.21 As is set out in the Executive Summary, the Review considers that it is important that the principle of taxpayers remaining responsible for their own tax affairs is maintained. Nevertheless, the effects described above have combined to mean that it is now particularly challenging for many of those affected by the Loan Charge to pay it. Many individuals saw the income resulting from the loans as part of their general salary and spent it accordingly. Some may have used it as capital, but this was not the common experience relayed to the Review. The vast majority, we heard, did not expect to have to pay tax in the future and made little provision to pay it. In addition, and particularly for earlier years in the 1999-2019 period, the length of time in question that has passed means that many scheme users are now earning less than they were at the peak of their earning potential.

Elements of the financial design drew particular comment from affected parties

3.22 A number of the features covered above are parts of the financial design of the Loan Charge, including the stacking of years, and the cumulative impact of the interest rates.

3.23 The Review agrees that there was a case for incentivising people to settle by creating a Charge which was marginally higher than the settlement terms on offer. However, the nature of the Loan Charge, and its application to both Protected and Unprotected years, led to the 2017 settlement terms being significantly tougher than the terms offered previously – particularly by requiring Voluntary Restitution in relation to Unprotected Years.

3.24 This was particularly true for those individuals wishing to settle pre-2011 usage. The CLSO 1 opportunity, offered to people who wished to settle schemes used before 2011, pre-dated the judgment of the Supreme Court in *Rangers*. Given that the lower tribunals had found against HMRC, it is plausible to expect many of those affected chose not to settle in view of the continued legal uncertainty at that point as to the tax treatment of loans.

Recommendations

3.25 This report goes on to consider the 'look back' period in more detail in the next chapter, and relevant recommendations are made there. With regards to the other design features, the Review makes the following recommendations.

3.26 The stacking of years, so that salaries received as loans across – in some cases – many years are taxed as if they were all paid in one year, is clearly very unusual. It means that, because of the Loan Charge, some taxpayers will pay tax at a higher rate than they ordinarily would. **The Review recommends that affected taxpayers should be able to choose not to stack their outstanding loan balances into a single year. They should be able to choose whether to spread the outstanding loan balance over a period of three years.**

3.27 This will give greater flexibility to those subject to the Loan Charge and reduce the risk that they have to pay at a higher tax rate than would otherwise be the case. This will particularly benefit those who used schemes for a limited period, and those earning lower sums in the relevant tax years.

3.28 In light of the cumulative impact of the interest rates – given the life changing amounts at stake and the length of time for which certain investigations were kept open with limited contact with taxpayers – **the government should review its future policy on interest rates within the tax system and report the results to Parliament by 31st July 2020.**

Chapter 4

Ability to look back 20 years

4.1 The element of the Loan Charge's design which has caused the greatest debate is its ability to look back over a 20 year period: the Loan Charge applies to loans that are outstanding on 5th April 2019, but which could have been taken out as far back as 1999. As already noted, this has also been referred to as 'retroaction' or 'retrospection'.

4.2 In assessing this element of the design, the Review has sought to balance fairness to the wider taxpaying population against the fair treatment of those who used loan schemes. The view put forward by HMRC that outstanding loan balances from schemes entered into as far as back as 1999 should be treated homogenously both:

- **relies on an assumption of clarity around whether schemes work** – it assumes it was always clear that the use of loan schemes was tax avoidance and would be treated as such. As is set out in Chapters 1 and 2, this was not consistently clear, with the courts not agreeing until the mid to late 2010s with HMRC's view of the taxable nature of schemes

- **cuts across standard practices** that aim to give taxpayers a degree of certainty about their past financial affairs, as recognised through the usual statutory limits within which HMRC can investigate a tax return

Whether tax was due on schemes used before December 2010 was highly disputed

4.3 In evidence to the Review, the government justified introducing the Loan Charge by saying that the tax payable under the Loan Charge was always due under the existing laws at the time, and that HMRC had always made this clear. If one accepts the government's view that the tax was always payable from the full range of years in-scope of the Loan Charge, then the Loan Charge is simply a mechanism which allows HMRC to collect outstanding taxes in an effective way.

4.4 However, this position was strongly disputed. Certainly until December 2010, many of those who have used and who have advised on loan schemes would not agree that the tax was payable on the loans. Their view was that the schemes (if properly implemented) achieved their aim of avoiding an income tax charge on the loan payment. HMRC did not establish their position in law until the 2011 legislation, and, for pre-2011 loans, the *Rangers* case in 2017. The 2011 legislation is consistent with this view as it did not tax existing loans, only new loans made to employees.

4.5 As set out in earlier chapters, though HMRC did investigate and then litigate cases from 1999 onwards, there was no conclusive win for HMRC until many years later. HMRC was not successful in proving its stated position in the upper courts until 2015 when the Court of Session found in favour of HMRC in the *Rangers* case, which looked at payments made between 2001 and 2009. The earlier tribunals (in 2012 and 2014) had found in Rangers' favour, and other cases were also found in favour of the taxpayer at this time or were inconclusive. Given that HMRC had not been able to prove their view in court, it is reasonable for a scheme user to take the position that a loan scheme could work, at least until December 2010. They would still, of course, need to disclose the details to HMRC and be prepared for the scrutiny that could follow.

4.6 Because the position of those schemes used before 2011 had not been made definitively clear by the Courts by the time the Loan Charge was announced, many of those who had used loan schemes believe that the Loan Charge denies access to justice by applying regardless of whether HMRC opened an investigation into their tax affairs, and regardless of whether their scheme usage falls within the legal principles decided in *Rangers*. The scheme user effectively no longer has the opportunity to present their case to a judge and potentially win the argument. This is a deliberate feature of the Loan Charge.

4.7 Following the decision in *Rangers*, HMRC now has the ability to issue Follower Notices in connection with many loan schemes entered into before 2010 (provided that HMRC protected the relevant tax years at the time or are now able to open an investigation), to seek to collect the tax due from employers in relation to those schemes. HMRC's evidence to the Review has been that over 3,200 Follower Notices have been issued in relation to loan schemes, with the vast majority following the *Rangers* case.

4.8 Given the lack of clarity from HMRC or support for their position from the courts before the 2011 legislation, the Review believes that using the standard approach for litigating, on a timely basis, is appropriate for pre-December 2010 loans, rather than the additional powers in the Loan Charge. This ensures that HMRC can continue to pursue schemes where it has been proven that tax is payable, without overriding the usual taxpayer protections.

4.9 The Review supports the use of *Rangers*, and other relevant judgments, to allow HMRC to pursue loan schemes entered into by both employers and individuals before 9th December 2010, should it wish to do so and where the legal principles established in the relevant caselaw apply. It should not, however, be able to apply the leverage of the Loan Charge in doing so. In keeping with the usual statutory position, HMRC will be able to recover tax from such cases when they opened an investigation and so protected a relevant year. Based on figures provided to the Review, this will be the case for approximately 60% of the tax years in question.

The position was clearer from December 2010 according to legal, expert, and contemporaneous commentary

4.10 As set out in Section A, there is a high level of consensus that 2010 marked a significant change in government rhetoric and action around loan schemes. While the position of loan schemes before 9th December 2010 is disputed, the view of most tax advisers and professional bodies we heard from is that the 2011 legislation is effective in ensuring that income paid through loan schemes is subject to tax.

4.11 The evidence given to the Review was consistently that once the new legislation was introduced, reputable advisers advised clients against using a loan scheme. In short, their view was that, following the 2011 legislation, schemes entered into on or after 9th December 2010 would clearly generate an income tax consequence.

4.12 The Review found this evidence convincing, noting as covered in previous chapters that it was also reflected in expert commentary at the time.

4.13 This view is also supported by a decline in usage of loan schemes after 2010-11, as shown in data provided by HMRC to the Review and shown in Chart 1.A earlier. Usage of loan schemes later increased again despite the new legislation, but we take this initial decline in their use, alongside testimony stating that a number of tax experts started to recommend against using schemes, as indicating that a number of scheme users probably changed their practices as a result of the legislation. This was reflected to a limited degree in impact statements received by the Review, with some scheme users noting that they had ceased using schemes following the 2011 legislation.

4.14 It is therefore the conclusion of the Review, as covered in Chapter 2, that the effect of the announcements and 2011 legislation was that it became legally clear that a tax charge would arise on income paid to employees through a third party from 9th December 2010.

The Loan Charge and taxpayer protections

4.15 In determining how far back the Loan Charge can fairly apply, the Review also noted that the time at which it became clear in law that the tax is due – over late 2010 and early 2011 – is also close to how far back HMRC would usually have been able to look in their investigations from the date of the announcement of the Loan Charge in March 2016. It is also more in line with the five year period that self-employed people are required to retain detailed financial records.

4.16 There are time limits for investigations in the tax system to help ensure that taxpayers have a degree of certainty in their financial affairs. HMRC has the right to ask questions about any Self Assessment tax return, but specific limits apply. After a certain number of years have passed, the tax year is regarded as one which is no longer at risk of an investigation.

4.17 These time limits are established in the Taxes Management Act 1970 and are an important feature of the tax system. They allow taxpayers to have certainty about the status of their tax affairs for earlier tax years. The time limits in the tax system can change, but such alterations would require primary legislation, be made overtly, and generally would be prospective only.

4.18 One of the submissions sent to the Review noted that "these statutory safeguards are part of the delicate balancing act laid down by Parliament to ensure that the Exchequer's right to revenue (i.e. the amount due under the law) is balanced by a taxpayer's right to finality and they should not be cast aside lightly". The Review agrees with this view. The taxpayer should, however, also meet their side of the implicit bargain and ensure that reasonable disclosure is made of their tax affairs to enable HMRC to open an investigation where justified for them to do so.

Box 4.A: HMRC's investigative time limits and Unprotected Years

HMRC has the power to enquire into any Self Assessment return within 12 months of the date on which it is submitted.

When that time has passed, they can issue a Discovery Assessment within strict time limits, the length of which is linked to someone's behaviour when completing their return.

HMRC has:

- 4 years, from the end of the tax year in question, to issue a discovery assessment under a wide range of circumstances
- 6 years, if a taxpayer was careless
- 12 years, if the issue arises from offshore non-compliance
- 20 years, if the action was deliberate (generally understood as fraudulent)

If HMRC open an Enquiry or issue a Discovery Assessment (referred to collectively by the Review as an investigation), then the tax year is described as protected.

If HMRC do not open an investigation within the time limits, then it is described as an Unprotected Year.

4.19 With regard to existing taxpayer protections, no distinction was drawn – in both the Loan Charge and 2017 settlement terms – between Protected and Unprotected Years.

4.20 The Review requested evidence from HMRC about the volume of Unprotected Years for schemes used both before and after December 2010. Absent the Loan Charge, HMRC would be unable to recover tax from these years (even through applying relevant judicial rulings such as *Rangers*).

4.21 Based upon a statistically significant sample of scheme usage which has already been settled with HMRC, approximately 40% of years that would otherwise be within scope of the Loan Charge prior to the start of the 2011-12 tax year are unprotected.

4.22 This figure is broadly consistent for both individuals – where HMRC consider that 40% of pre-2011 scheme usage took place in an Unprotected Year, and employers – where HMRC consider that 30-45% of pre-2011 scheme usage took place in an Unprotected Year. This reflects the fact that, for a very significant minority of loans entered into before 9th December 2010, no investigations (either enquiries or assessments) were opened by HMRC into the tax affairs of the scheme users involved, and so the users were never put 'on notice' of HMRC's interest in their tax affairs. Where HMRC did open investigations within the statutory time periods, and where the legal position permits, HMRC are able to apply relevant judicial rulings (such as *Rangers*) in order to recover the tax that is due.

4.23 For loans entered into from the 2011-12 tax year onwards – based again upon a statistically significant sample of scheme usage already settled with HMRC - 10-15% of years are unprotected for individuals, and 10-25% for employers. The evidence from HMRC was that this volume of Unprotected Years arose primarily from a lack of disclosure of loan schemes. Disclosures both of loan schemes under DOTAS – and from scheme users – fell particularly sharply from 2014 onwards after the introduction of APNs, which enabled HMRC to more quickly recover tax payable on schemes. Disclosure levels had, however, declined after the 2011 legislation as a result of the tax consequences clearly arising on loan schemes.

4.24 At the request of the Review, HMRC conducted a review of a sample of Unprotected Years for post-December 2010 scheme usage which has already been settled. This found that – even under a generous definition of which schemes had been disclosed to HMRC[1] – under 4% of Unprotected Years occurred when disclosure had been made. The Review engaged the Government Internal Audit Agency (GIAA) to independently consider the work conducted by HMRC. They concluded that, given the circumstances under which HMRC undertook their analysis, the approach and methodology applied was not unreasonable and broadly supported the conclusions reached by HMRC from the data which was available to them. However, GIAA advised that – given the data was taken only from settled cases – they were unable to confirm whether the level of non-disclosure was consistent across the total affected population, including taxpayers who would ultimately pay the Loan Charge. GIAA nevertheless considered that the data offered a good proxy and found no evidence to indicate that non-disclosure levels are different amongst the wider population.

4.25 Where reasonable disclosure has been made, the Review agrees that Unprotected Years should be outside the scope of the Loan Charge. However, any other Unprotected Years should remain in scope. Removing all Unprotected Years from the scope of the Loan Charge would, in effect, ensure that scheme users who disclosed their schemes to HMRC paid higher tax bills than scheme users who did not disclose. This would set an unacceptable precedent within the tax system, and risk incentivising future non-disclosure to HMRC. On balance, the Review considers that the harm that would be caused by this outweighs the consideration that should be given to preserving the usual protections afforded to taxpayers.

4.26 There are, however, a limited number of cases in which a scheme user made reasonable disclosure of their usage of a scheme to HMRC but no investigation was opened by HMRC. In these cases it is right for the usual statutory position to prevail, and for HMRC to be unable to open an

1 Meaning that reference had been made on a tax return to income being received via a loan, even if a DOTAS scheme reference number had not been included

investigation if they are now outside the usual time limits for doing so. From March 2016 onwards – when the Loan Charge was announced – HMRC made a reasonable assumption that they need not continue protecting years in which they identified usage of loan schemes. Unprotected Years from the start of the 2016-17 tax year onwards should therefore continue to automatically be within the scope of the Loan Charge.

4.27 The Review is therefore recommending that scheme users who entered into loans between 9th December 2010 and the start of the 2016-17 tax year, and who: (i) can evidence reasonable disclosure of their usage of a loan scheme to HMRC via a tax return; and (ii) that HMRC did not protect the relevant tax year, should have that Unprotected Year taken out of scope of the Loan Charge. Outside of these circumstances, Unprotected Years should remain in scope of the Loan Charge.

4.28 For these purposes, a "reasonable disclosure" should be considered as not requiring the submission of a Scheme Reference Number (where a scheme was registered under DOTAS), but build upon HMRC's ordinary compliance approach in considering the extent to which a Self Assessment Return is sufficiently clear about the usage of a loan scheme.

People still received misleading professional advice after 2010

4.29 In making its recommendations, the Review is conscious that taxpayers may have still entered into a scheme on or after 9th December 2010, and not understood that tax would be considered due. We received a large volume of evidence that individuals did not understand at the time that the schemes would be considered tax avoidance and would have not used them if they did. Many people affected by the Loan Charge clearly feel a real stigma through being associated with tax avoidance, which is exacerbated through not having understood the nature of loan schemes.

4.30 Many taxpayers in this category entered into loan schemes because a professional adviser presented them with the arrangement and suggested it was suitable for them to use. This came through strongly from those the Review met and in the impact statements we read. The Review has a great deal of sympathy with people who relied upon professional advisers in determining how to structure their financial affairs, and notes that the increasingly mass-market nature of loan schemes has created a large pool of potential customers for unscrupulous advisers.

4.31 The Review also heard that people may have been induced into using schemes, or had schemes recommended by reliable third parties. Examples of such behaviour included individuals being made redundant and told that they needed to use a specific umbrella company and a specific loan scheme if they wanted to be re-engaged. A more common example involved individuals being presented with a list of umbrella companies which could act as employers, one or more of which also involved the use of a loan scheme. Such lists did not make clear which umbrella companies were associated with loan schemes, meaning that scheme participants may not have understood the nature of the arrangements.

4.32 Based on evidence received, the Review is not able to reach a judgement as to how frequent these practices were, or what proportion of the population directly affected by the Loan Charge fall into these categories. Given the passage of time since taxpayers entered into schemes, it is not in any event possible to make any such assessment on a case-by-case basis.

4.33 It is a fundamental principle of the tax system that people are responsible for their own tax affairs, even if they have been sold an arrangement which was inappropriate. Notwithstanding the sympathy that the Review feels for people who did not understand the nature of the loan schemes they were being sold, it is important that this principle remains in place. However, many of the recommendations in this report should help these individuals, particularly those who are now on lower incomes.

Recommendations

4.34 **The Loan Charge should not apply to loans made before 9th December 2010** given the broad consensus that Finance Act 2011 both made the government's position clear and prevented future loan schemes from achieving their aim. It is also approximately how far back HMRC would have been entitled to look under the normal operation of the tax system at the point that the Loan Charge was introduced.

4.35 This does not, however, mean that all loans prior to that date are definitively not taxable. In certain cases where a loan scheme has been used the tax year will be a Protected Year, meaning that HMRC is able to continue with its compliance and litigation activity without the Loan Charge overriding the existing rules. For such years, HMRC may be able to pursue the tax owed.

4.36 The inclusion of both Protected and Unprotected Years in the scope of the Loan Charge effectively overrides the usual statutory protections for taxpayers. Nevertheless, **the decline in disclosure of scheme usage post-2011, and the need to ensure non-disclosure is not incentivised, justifies the inclusion of Unprotected Years within the scope of the Loan Charge, except where reasonable disclosure of scheme usage was made to HMRC**. Any Unprotected Years arising from loan schemes entered into during the 2016-17, 2017-18 and 2018-19 tax years should all be included in the scope of the Loan Charge.

4.37 HMRC should refund relevant elements of settlements made since 2016 consisting of Voluntary Restitution paid in relation to Unprotected Years when the relevant loans were entered into:

- prior to 9th December 2010; or
- between 9th December 2010 and the start of the 2016-17 tax year, where the scheme user made reasonable disclosure of their scheme usage in their tax return

4.38 When repaying Voluntary Restitution, HMRC should ensure that this does not lead to any unintended tax advantages for those using loan schemes, including arising from any interactions with Corporation Tax or the withdrawal of transitional relief on investment returns announced at Budget 2016.

4.39 Given the principled nature of these recommendations, they apply to both individuals and employers within scope of the Loan Charge. This will align with the legislation establishing the Loan Charge in Finance Act (No. 2) 2017, which does not draw a distinction between the two.

Section C: Personal impact of the Loan Charge

In addition to the principles of how the Loan Charge should operate, the Review has been very conscious of the impact of the policy both on those directly affected by it and on their families.

This impact has, in certain cases, been exacerbated by a disjointed response by HMRC including in relation to both clarity and timeliness of communication.

This section of the report therefore sets out the individual impacts of the Loan Charge, beyond the elements of its design covered in earlier chapters. The previous recommendations should significantly alleviate pressure on individuals. However, given the particular impact of the Loan Charge, where there are still people who will struggle to pay there is a strong case for doing more to help the most vulnerable. The recommendations on payment are therefore deliberately designed to target this group as much as possible.

Key conclusions and recommendations

• whilst HMRC's powers have increased significantly, particularly with the Loan Charge, its performance and accountability has not increased at the necessary rate when compared to that accumulation of those powers

• anyone subject to the Loan Charge should only have to pay up to half their disposable income each year and a reasonable proportion of their liquid assets. No one should have to sell their primary residence or use their existing pension pot to pay the Loan Charge

• the government should set a maximum repayment period of 10 years for those with income of less than £30,000 a year, writing off whatever is still owed at the end of 10 years of paying an instalment arrangement. This will ensure that taxpayers are able to draw a line under their use of a loan scheme and move on

Chapter 5

What people told us about the impact of the Loan Charge

5.1 This chapter summarises who is affected by the Loan Charge, and what they told us about that impact, before the report goes on to look at the issues of affordability, implementation, and those who promoted or sold the schemes in detail.

Who is affected by the Loan Charge and how are they impacted

5.2 The number of people affected by the Loan Charge is contested, but HMRC estimate that 50,000 individuals are directly impacted by it. There are an additional 10,000 employers affected.

Box 5.A: Distinguishing between individuals and employers

The evidence from HMRC is that at least 78% of the 10,000 employers affected by the Loan Charge are close companies i.e. ones usually controlled by a small number of people. These employers typically entered schemes on professional advice from financial advisers or scheme promoters.

3,200 settlements have been entered into by employers, meaning the remaining 6,800 identified cases have not settled.

Cases where the employer cannot pay their liabilities from the Loan Charge (including as a result of having been dissolved) will result in the liability arising on the owner/managers of the employer and – in certain circumstances – directly on the employees. The nature of the Loan Charge liability means that it can arise on owner/managers of dissolved companies in a way that goes beyond other elements of the tax system which permit transfers of liabilities in more limited circumstances.

As the Loan Charge primarily constitutes an income tax charge, the net effect of a tax liability falling on an employer is therefore largely for it to be passed through to individuals, with the employer (where it exists) being used as a conduit for settling via PAYE.

As a result, the Review considers that the distinction between employers and individuals is not a helpful one, and the recommendations in this report cover both except where specified. This is consistent with the legislation establishing the Loan Charge, which does not distinguish between employers and individuals.

5.3 The Loan Charge does not generally fall on large employers. Most large employers exited these schemes and settled before 2016, lending credence to the argument that those who could afford expert advice following the 2011 legislation were convinced of the fact that these schemes no longer worked. There is also no simple stereotype of the type of person affected by the Loan Charge, and they are not the 'usual suspects' that people think of as avoiding tax.

5.4 Over 700 impact statements were given to the Review, mostly through the LCAG and the Loan Charge APPG. We are grateful for the candour of all those who submitted an account of their experiences.

5.5 They were considerable in number, but we make no judgement about how representative they were of the entire population of those affected. In coming to our conclusions, we have compared what we heard from impact statements to the other evidence we received, including copies of documents and expert testimony. Further detail of our approach to analysing the evidence can be found in the Annexes.

5.6 The majority of the impact statements said that the author, or a family member, had experienced a decline in their mental health as a result of their experiences with the Loan Charge. Many also referenced the strain on relationships and impact on other family members. We hope that those dealing with mental health issues are able to access the many sources of support available.

5.7 A lower, but still considerable, number referenced suicidal thoughts. The LCAG and the Loan Charge APPG have, at the time of writing, said that seven people affected by the Loan Charge have taken their own lives. HMRC have stated that where they are aware of having recent contact with someone who has taken their own life, the case is referred to the Independent Office for Police Conduct. The Review understands that there can be many causes for someone taking their own life and does not wish to overlook the potential complexity. Any instance of someone taking their own life is clearly devasting for family and friends, and we thank those brave individuals who told us about the personal impact that deaths of family members had on them. We are also grateful to those who submitted their accounts through the Loan Charge APPG and respect their desire for anonymity. Our condolences go to all those who have lost someone in this way.

Chapter 6

The personal impact of implementation

6.1 One of the common themes across many of the impact statements submitted to the Review was that the negative experiences of those submitting came not just from the need to pay significant sums of money, but also from the experience of how cases were handled by HMRC.

HMRC's performance

6.2 In this chapter, the Review sets out those experiences. Our view has been guided by the principle that the government must ensure that HMRC's increased powers are matched by greater accountability and improved performance, in recognition of the impact that they can have on members of the public.

6.3 It should be acknowledged that it is, understandably, more likely for people to contact the Review when they have had negative experiences. Those with positive or neutral experiences would have less incentive to contact the Review. However, there is enough evidence to illustrate that the way in which HMRC dealt with some individuals fell short of the standards that the taxpayer might reasonably expect.

Unclear settlement calculations

6.4 The Review heard of difficulties in knowing or understanding the amount HMRC considered due. We received repeated accounts of HMRC providing figures that were inaccurate, either by being internally inconsistent or because they were very significantly higher than the result of similar calculations conducted by the individual or their accountants – in some cases by tens of thousands of pounds.

6.5 The fact that the Loan Charge could look back 20 years also made it less likely that scheme users would have kept financial paperwork, therefore making it harder for them to challenge those calculations. In certain cases, this contributed to taxpayers providing HMRC with additional relevant information as cases developed – leading to further calculations of sums owed through settlement, and consequential delays in settlement being agreed.

6.6 In addition, the amount of leverage that HMRC had to make people settle – given that the alternative to settling would be paying the Loan Charge - makes these reports particularly troubling as it could make it more likely that people will settle for amounts that exceed what they truly owe.

Delays in responding

6.7 The impact statements referenced the difficulty and delays in finding out whether a settlement offer had been agreed with HMRC. Many impact statements related experiences of suggesting a settlement to HMRC before waiting some months for a reply. They would then be asked to respond to HMRC very quickly. Evidence received by the Review was that some taxpayers experienced this on a repeated basis, prolonging the personal impact of going through settlement.

6.8 In certain cases – particularly where HMRC took many months to respond to offers of settlement or to communicate with people affected – the Review considered that HMRC's performance was unacceptable, and fell far below the standards that taxpayers can reasonably expect.

Lack of a coordinated response

6.9 The evidence submitted to us also described the impact of a lack of a coordinated response between different parts of HMRC, such as those dealing with APNs and separately with the Loan Charge.

Examples included timelines provided to the Review where the person had calls and visits from HMRC asking them to pay an APN, when the individual had already proposed a settlement to HMRC, and asked HMRC to work through their appointed tax adviser. Those parts of HMRC asking for payments from the person seemed unaware of the arrangements or the settlement offer. Similar themes recurred throughout much evidence submitted to the Review, reflecting a disconnect between different parts of HMRC.

Poor communication

6.10 The Review received repeated evidence of HMRC opening an investigation, but not subsequently updating the taxpayer into whose affairs an investigation had been opened. HMRC consider cases where an investigation has been opened to be protected, unless an individual taxpayer successfully applies for them to be closed. When combined with HMRC's early strategy of focusing on one lead case, gaining a clear legal position, and then collecting tax from other users of the same scheme, the Review found that scheme users could easily have received a single generic letter saying that an investigation had been opened into their affairs, and then no direct contact for many years afterwards.

6.11 Not unreasonably, the taxpayer would at some point expect that the case was closed, when it was in fact not. As a matter of law, HMRC would have protected the year in question, enabling them to return to their investigation at a later date. But the experience for the taxpayer was frequently one of surprise that their affairs were still under investigation, and that HMRC had not been in contact with them in the intervening period.

6.12 HMRC's strategy until around 2014 relied on communicating with promoters or advisers. This may have worked with larger employers, but arguably HMRC should not have assumed promoters and employers established to facilitate a loan scheme would provide updates to individual scheme users. HMRC's historic approach also left it open for the promoter to control what individual scheme users thought was happening with HMRC's investigation.

6.13 HMRC's approach since 2014 has evolved significantly. The Review received evidence from HMRC of a more active approach, based on greater access to Real Time Information. This approach, which the Review welcomes, better enables HMRC to communicate directly with individuals at an early stage about their potential involvement in tax avoidance.

6.14 We also received accounts of individuals finding letters or visits from HMRC to be unnecessarily threatening, intimidating or embarrassing.

Conclusions

6.15 The result of these experiences is that trust has broken down between HMRC and a large number of those we heard from. The Review heard about how charities and HMRC already address similar issues, including in evidence from TaxAid and the Low Incomes Tax Reform Group. The Review was particularly grateful for the expert input provided by charities of this type, and noted the significant role that they have in providing advice to vulnerable taxpayers in a dispute with HMRC. The expansion of this sort of advice, including through additional funding being provided, would allow taxpayers affected by the Loan Charge to better assess the full range of options available to them, including the suitability of an individual voluntary arrangement (IVA) or other forms of debt restructuring.

6.16 Taken together, the Review concludes from this testimony that whilst HMRC's powers have increased significantly from 2000, including with the Loan Charge, HMRC's performance and accountability have not increased at the necessary rate when compared to that accumulation of those powers.

HMRC's accountability to taxpayers

6.17 As was noted by the EAC last year, a number of organisations - including Parliament, HMT, the courts, the National Audit Office, and the Adjudicator's Office – all have oversight of elements of HMRC's work. None, however, have general oversight of HMRC's treatment of taxpayers. It is concerning that the themes highlighted above have also been identified elsewhere, including in the Adjudicators' Office most recent annual report.[1]

6.18 Themes identified by the EAC include the risk of HMRC staff having been pressured to "take a more aggressive approach to tax collection", and certain HMRC staff displaying aggressive and unreasonable behaviour towards taxpayers. Similar issues were raised by people giving evidence to the Review. Our attention was also drawn to the risks of HMRC and taxpayers becoming entrenched in a dispute over the level of tax that is due, as a result of a lack of confidence in how tax is being calculated, and delays in the settlement process. Similar findings have been reported by the Adjudicator's Office, including that "delays, along with a perceived lack of empathy by HMRC had fuelled customers to complain and to continue to escalate their complaint."

6.19 The nature of HMRC's engagement has contributed both to Parliamentary concern, and the level of frustration experienced by many people. HMRC's service levels need to continue improving, and there are lessons to be

1 The Adjudicator's Office provides an independent review of complaints about HMRC. The Adjudicator's Office (2019) Annual Report 2019 is available online.

learned from other reports that have identified the need for HMRC to better communicate with the public, and to respond flexibly to the circumstances of individual taxpayers.

6.20 HMRC's evidence to the Review has highlighted the support that the department provides, including through its Additional Customer Support programme, the enhanced payment arrangements made available in connection with the Loan Charge, and through training frontline staff to identify taxpayers in need of extra help.

6.21 There is a clear disconnect between HMRC's view of this support, and how it has been experienced by some of those affected by the Loan Charge. However, if HMRC's approach of communicating more directly with the public is to be successful, they must continue building trust through interactions with taxpayers. The UK benefits from high levels of voluntary compliance with the tax system, which is essential to facilitating tax collection. This speaks to the need for HMRC to think more widely and deeply about how it communicates, and indeed to start to consider itself more fundamentally as a communications department.

6.22 Delivering this change in approach will require sustained focus. The recommendation from the EAC that the recently established Customer Experience Committee brings together input from the major tax bodies, Adjudicator's Office, and representatives of taxpayer groups to better challenge HMRC would go some way towards ensuring continued emphasis on this issue.

6.23 Evidence received from representative bodies, including the Institute of Chartered Accountants in England and Wales (ICAEW) and Chartered Institute of Taxation (CIOT), highlighted that many of the concerns about the Loan Charge – particularly around its ability to look back 20 years and consequential impact on individuals – were raised by representative bodies soon after Budget 2016.[2] Had the views of such groups been better considered in implementing the policy, it is likely that at least some of the concerns raised by taxpayers would have been addressed.

Recommendations

6.24 HMRC has a duty to collect revenue. It must be able to reach settlements with those who it considers to owe tax, in order to be fair to the wider taxpaying population. This includes securing the best return to the Exchequer, which should mean collecting the right amount of tax due rather than seeking to secure the maximum that might be collectable.

6.25 However, taxpayers subject to the Loan Charge also have reasonable expectations about how they should be treated. These should reflect the enhanced responsibilities that HMRC has as a result of their increased powers.

2 ICAEW representation 150/16 described the proposals as "aggressively retroactive against taxpayers who have not done anything that would under current rules leave themselves open to a 20 year assessing window which currently requires HMRC to demonstrate that there has been a deliberate accuracy in a return".

CIOT's response to HMRC's technical consultation of October 2016 described the proposals as "effectively impos[ing] a retrospective tax charge on events that happened in the past".

6.26 Examples of reasonable expectations which the Review does not consider to have been met for taxpayers affected by the Loan Charge include:

- yearly updates on the status of enquiries as it is reasonable to expect an issue to have been closed after not hearing an update for a year
- openness so that an individual understands why they may owe tax, how much HMRC considers to be owed, and how that figure was calculated
- join up between different parts of HMRC in their messaging and understanding of the details of a case, so that the communications are accurate and do not change over time due to oversights such as a failure to include amounts owed under different taxes
- an appropriate tone and approach in interactions with loan users, particularly calls and visits, so that HMRC can collect tax but is not unnecessarily insensitive in the way that it does so

6.27 To ensure that these reasonable expectations are met, **HMRC should report to Parliament on its implementation of the Loan Charge**, drawing on the recently established Customer Experience Committee, feedback from representative bodies, charities aimed at providing tax advice to low-income individuals and other professionals. This report should also address common themes arising from other recent reports, including from the EAC and the Adjudicator. HMRC should do so as soon as possible and before the end of 2020, at the latest.

6.28 **HMRC's Charter should also be reviewed** to set higher expectations of performance during interactions with members of the public, and to ensure that staff are trained to meet these expectations.

6.29 **HMRC should update taxpayers at least annually about the status of open tax enquiries** (except where doing so would risk alerting a taxpayer to a criminal investigation) and highlight that they have the option to request that these be closed. Where this does not take place, the non-communication should be taken into account by the FTT if a taxpayer applies to have an open enquiry closed.

6.30 HMRC should fund an external body to provide independent advice to lower income taxpayers who are discussing payment arrangements and debt collection with HMRC. This will help to maintain trust in future, ensure that HMRC set out their position clearly, and support scheme users to better understand the range of factors that are taken into account when making decisions.

Chapter 7

Affordability for individuals with a lower ability to pay

7.1 The Review considers it important that those who have a lower ability to pay are not disproportionately affected by the abnormal design of the Loan Charge.

7.2 A lot of the personal testimony that the Review received spoke of the difficulty of paying the amounts expected under the Loan Charge or a settlement under the 2017 terms, reinforcing the importance of considering this issue. We heard from people whose income had changed since they used the schemes, such as those who had retired, and from people whose careers would suffer if they were declared bankrupt, including those working in financial services. People in these categories do not make up the full population of those affected by the Loan Charge, but are nevertheless a significant proportion of those affected.

7.3 The government has been clear that it does not want to force people into bankruptcy or into selling their main home as a result of the Loan Charge. It is not, however, clear to the Review whether or how this intention can be delivered in practice. The sums of money at stake make it likely that some of those facing the Loan Charge will enter into bankruptcy or sell their home. While HMRC has already made concessions aimed at supporting people to pay, we found that the mitigations already provided by HMRC, whilst welcome and significant, need to go further.

7.4 Our recommendations, deliberately aimed at those on lower incomes, should help to achieve those aimsbeyond the impacts that other recommendations – particularly relating to the extent of the look-back period within the Loan Charge and income stacking – will have.

Everyone should pay their fair share of tax, but the payment arrangements also need to be affordable

7.5 The Review's previous recommendations are aimed at correcting the principled issues with the design of the Loan Charge, bringing it closer in line with the wider tax system. We have found that there is a case for the Loan Charge to be in place for loans entered into from 9th December 2010, and so taxpayers who entered into schemes from that date will need to pay the Loan Charge. HMRC's evidence, set out more fully below, is that approximately 40% of people who exclusively used schemes from the 2011-12 tax year onwards and have not yet settled their tax affairs had a 2017-18 income of less than £30,000.[1]

[1] This chapter primarily refers to individuals who entered into schemes from 2011-12 onwards, rather than from 9th December 2010 onwards. This reflects the data provided by HMRC, which is typically divided by the year in which loan schemes were entered into.

7.6 In determining how this population should pay the Loan Charge, the Review is clear that everyone should pay their fair share of tax in order to fund public services. HMRC are therefore right to try to ensure that no one benefits from tax avoidance.

7.7 In practice, however, it is only possible for people to pay what they can afford. HMRC have already been clear that those settling instead of paying the Loan Charge should not be required to sell their primary residence in order to settle their tax liability. The Review considers that people with income of less than £30,000 who will be required to pay the Loan Charge should be able to do so over a time period that will, regardless of the amount owed, be able to give them a clear end date beyond which they will not need to continue paying the outstanding sum. We are recommending that this be calculated on the basis of reported income to HMRC in 2017-18, so as to ensure that no incentives are created for under reporting of income.

The abnormal design of the Loan Charge can create unaffordable cases

7.8 The Review found that the current unusual design of the Loan Charge, particularly the length of time that it looks back, can create some cases where the amount owed can be exceptionally large and someone's financial situation is more likely to have changed (though our recommendations to reduce the look back period would improve this situation).

7.9 For example, the Loan Charge's current ability to look back over a number of years, and the inclusion of Unprotected Years, can create situations where someone who now has a lower income owes a very large amount. A low paid agency worker, for example, could have used a scheme for a decade, accumulating a large amount of tax that they now owe. Such experiences would not be typical; the evidence provided by HMRC was that of individuals who used a scheme from the 2011-12 tax year onwards, 70% did so for two or fewer years and only 16% used a scheme for four or more years. The length of the look-back period, however, creates potential for many years' usage of schemes to be taxed in a single year. The point was also frequently made that scheme users' circumstances are more likely to have changed during the 20 year look back period, such as through reduced earning potential or retirement. For example, 43% of respondents to the Loan Charge APPG survey, which received over 1,700 responses, were aged over 50, and may be more likely to have passed the potential age at which their income will have peaked.[2]

7.10 Alternatively, of course, a highly paid company director could have used a scheme to increase their earnings in a single year, and therefore owe relatively little whilst still earning a large amount.

7.11 In short, there is not an absolute, one-to-one link between how much someone owes and their current ability to pay it. The result is that in some cases, but likely not the majority, people can owe considerably more than they can afford to pay, compared to their disposable income.

2 'Loan Charge Inquiry: Survey Results', All-Party Parliamentary Loan Charge Group, 2019

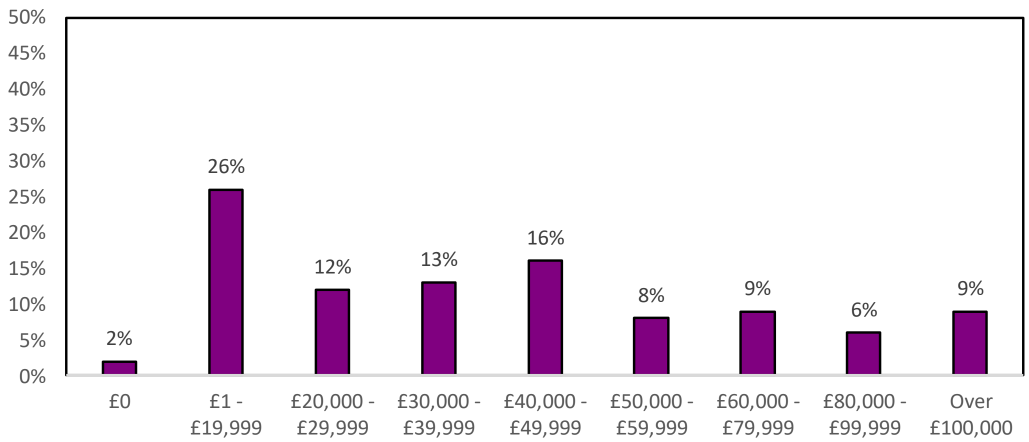
Those affected by the Loan Charge are not the 'usual suspects', but as a group are better off than the general population

7.12 Those people facing the Loan Charge are not who the public might perceive as the 'usual suspects', meaning large international corporates or very rich individuals receiving sophisticated tax advice. Large corporates settled when they saw that the schemes were unmistakably not viable after the 2011 legislation and are therefore not subject to the Loan Charge.

7.13 The residual group, many of whom have not entered into settlements with HMRC, are generally on mid-range or lower incomes, coming from industries like IT, construction, and financial or business services.

7.14 According to HMRC, approximately 40% of relevant scheme users had income in 2017-18 below £30,000, which is slightly above the median national salary for a full-time employee. This is set out in Chart 7.A.

Chart 7.A: Approx. 40% of scheme users who exclusively used schemes from 2011-12 onwards reported income of less than £30,000 in 2017-18



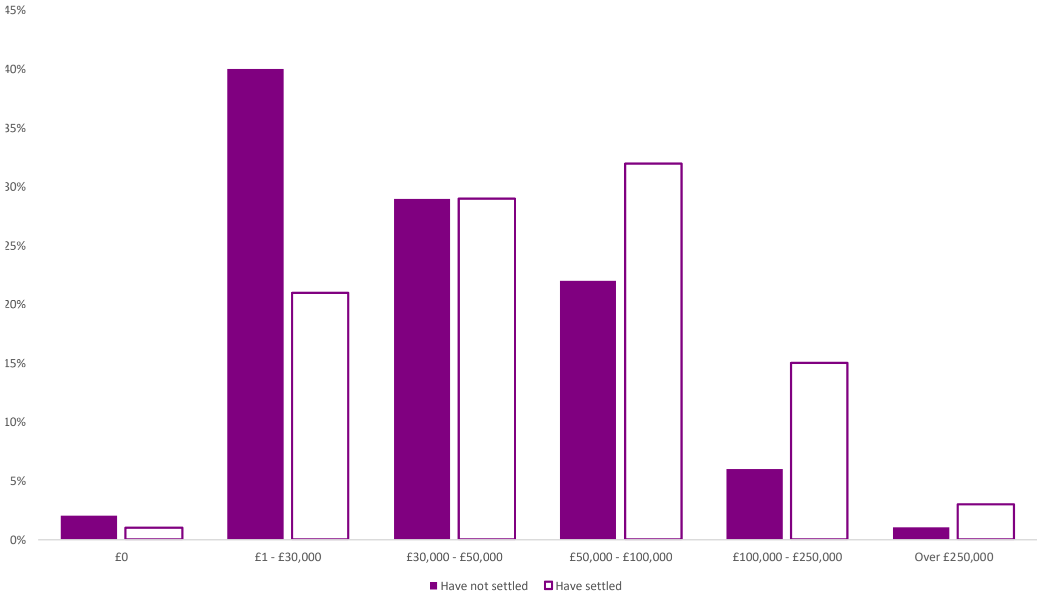
Source: HMRC PAYE, Self Assessment, and operational data for 'individuals who used loan schemes'[a]

a Chart 7.A shows reported incomes in 2017-18 for individuals who exclusively used schemes from 2011-12 onwards, excluding those who used schemes in 2017-18 as the reported incomes for such scheme users will be artificially reduced. Certain individuals used schemes both before and after 2011-12, and are not reflected in this data.

7.15 Chart 7.B demonstrates that relevant scheme users who have settled with HMRC typically have higher incomes than those who have not. 42% of scheme users who have not settled had reported income of under £30,000 in 2017-18, compared to 22% of those who have settled.

7.16 A similar pattern exists for the population of individuals who entered into loan schemes in the period from 1998-99 to 2011-12. Although the Review is recommending that taxpayers who entered exclusively into loan schemes prior to 9th December 2010 are removed from the scope of the Loan Charge, these trends provide a degree of support for the perspective that those who can readily afford to settle rather than pay the Loan Charge are likely to have chosen to do so. Doing so will also have settled the underlying tax liability, whereas paying the Loan Charge will mean that the underlying liability will continue to exist (to the extent that it has not been paid by paying the Loan Charge).

Chart 7.B: 42% of scheme users who have not settled and exclusively used schemes from 2011-12 onwards reported income of under £30,000 in 2017-18, compared to 22% of those who have settled



Source: HMRC PAYE, Self Assessment, and operational data for individuals who used loan schemes[a]

a Chart 7.B shows reported incomes in 2017-18 for individuals who exclusively used schemes from 2011-12 onwards, excluding those who used schemes in 2017-18 as the reported incomes for such scheme users will be artificially reduced. Certain individuals used schemes both before and after 2011-12, and are not reflected in this data.

The Loan Charge can be affordable, more so for those who have higher incomes

7.17 The Review found evidence to suggest that settlements under the 2017 terms, and the Loan Charge are likely to be affordable for many of those affected.

7.18 For example, just over two thirds of those who have settled owed a sum that was less than or equal to their 2017-18 income, according to HMRC data.[3] Approximately one third of respondents to the Loan Charge APPG survey reported that the total amount they owed was a sum lower than, or equal to, their current income. These are imperfect measures of affordability but demonstrate the broad picture for those affected.

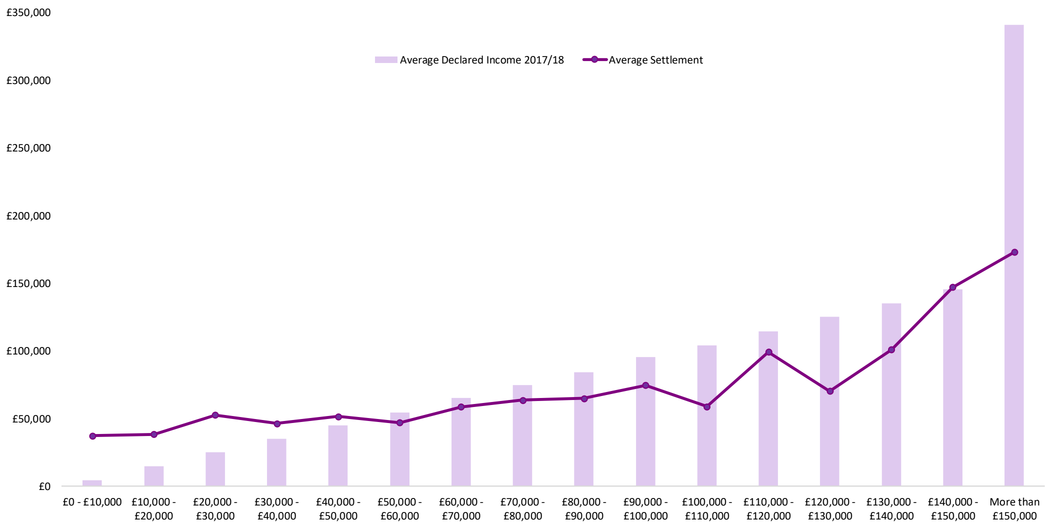
7.19 Chart 7.C, based upon data provided by HMRC, shows that on average those with higher incomes owed less than their 2017-18 income, making it more affordable for them than for those with lower incomes. As is set out in the chart, people with incomes of lower than £50,000 in 2017-18 typically had a liability greater than their 2017-18 income.

7.20 This analysis is based on anonymised data supplied to the review by HMRC for those who have settled under the 2017 terms. As previously discussed,

3 Anonymised data for 4,084 people was supplied by HMRC to the Review

those who have already settled tend to have higher incomes than those who have not settled. The relationship between income and amount owed may also differ, but the data was not available to establish whether this is the case. The data also includes those who used schemes before 2011, but the Review anticipates that it is generally indicative of how affordable the Loan Charge is for those with different income levels.

Chart 7.C: annual incomes (shown as bars) start to exceed the total amounts owed (shown as a line) as people earn more



Source: Data provided to the review by HMRC on 4,084 scheme users that have settled and their income is known to HMRC[a]

a Unlike Charts 7.A and 7.B, Chart 7.C refers to the incomes of scheme users who entered into loan schemes both pre and post the 2011-12 tax year.

7.21 In addition to income, someone's ability to pay is also determined by the assets that they have at their disposal. Data was requested on the assets those facing the Loan Charge have, but HMRC do not collect this data. We heard case studies ranging from people with no savings or housing equity and personal debts, to others with substantial property and financial wealth, but are unable to draw any broad conclusions.

Changes announced on payment arrangements are helpful, but more are needed

7.22 The government has already made a number of concessions in the payment arrangements, particularly for those due to pay under the 2017 settlement terms.

7.23 The Review was specifically asked to consider in its Terms of Reference whether those "changes announced by the government in advance of, and since, the Loan Charge came into effect address any legitimate concerns that have been raised about the impact on individuals, including affordability for those affected".

7.24 The Review has considered the following changes in particular. The introduction of automatic payment arrangements for those who settle:

- the government has introduced automatic payment arrangements for those who settle, with individuals with income of under £30,000 per year in 2017-18 having up to seven years to pay their settlement without needing to provide HMRC with further details of their asset ownership, and individuals with income of under £50,000 per year in 2017-18 having up to five years to pay

- the Review welcomes the introduction of the automatic payment arrangements, but notes that they have only been extended for individuals who settle

- While welcome, further payment arrangements will therefore be needed for each of individuals, employers, and individuals to whom employers' liabilities are transferred once the Loan Charge takes effect in January 2020

7.25 The Loan Charge not applying to a tax year where an enquiry was closed on the basis of fully disclosed information:

- the government announced in July 2019 that HMRC will not apply the Loan Charge to a tax year where an investigation was closed on the basis of fully disclosed information

- HMRC will be able to assess the number of cases in which this measure will apply following the Self Assessment deadline on 31st January 2020, as the relevant information to make decisions regarding individual cases has not yet been submitted to HMRC

- the Review agrees with the principle behind this concession and have built upon it through our recommendation, set out more fully in Chapter 4, that years which are unprotected in which scheme users made reasonable disclosure of their usage of a loan scheme to HMRC should also be removed from the scope of the Loan Charge

7.26 The additional flexibility announced in July 2019 for individuals settling who may be in genuine hardship:

- the additional flexibility announced by HMRC in July 2019 similarly only applies to individuals who settle with HMRC and are in genuine financial hardship as a result

- HMRC assess that it could potentially benefit a limited number of individuals, and will be able to confirm the precise number once settlement discussions are completed

- this change does not benefit either those people who are financially impacted as a result of the Loan Charge itself (of whom there over 35,000 outside the settlement process), or individuals who have their employer's liabilities transferred to them

- the Review therefore concludes that this measure does not go sufficiently far to address concerns over affordability of the Loan Charge itself

Recommendations

7.27 For the reasons set out above, the Review concluded that the changes already announced by the government are welcome, but have not gone far enough in ensuring that those who have lower incomes, and also have fewer liquid assets, are still able to pay the Loan Charge.

7.28 **Any individual subject to the Loan Charge should only be asked to pay up to half their disposable income each year and a reasonable proportion of their liquid assets; no one should have to sell their primary residence or use their existing pension pot to pay the Loan Charge**.

7.29 The Review is particularly concerned that there may be relatively lower earners who would need a disproportionately long time to pay the Loan Charge or be driven to bankruptcy or selling their main residence. In addition to the Time to Pay arrangements, we are therefore recommending that:

- **those individuals with income of less than £30,000 in 2017-18 should not have the Loan Charge hanging over their head for any longer than 10 years**
- **any amount left outstanding after 10 years of paying an instalment arrangement should be written off to genuinely draw a line under any outstanding balance. This will allow people to move on after paying their fair share**

7.30 In designing our recommendations, we aimed to deliberately target those with less. We have therefore set a qualifying 2017-18 income of £30,000 or less for individuals to be eligible for these terms.

7.31 Although approximately 40% of people who exclusively used schemes post-December 2010 and have not yet settled had income of less than £30,000 in 2017-18, a further 30% had income of £30,000-£50,000. Had these people settled with HMRC, they would have been eligible for the automatic payment arrangements described above and able to enter into a payment arrangement of up to five years without providing details of their asset ownership to HMRC. **The Review therefore recommends that these terms are similarly extended to people in this category who have not settled and will therefore pay the Loan Charge.**

7.32 The Review's recommendations around affordability are not intended to prolong artificially the time period over which individuals pay the Loan Charge. This would not be in the interests either of taxpayers or HMRC. Where individuals are financially able to pay the Loan Charge quickly (either up-front or through a brief payment arrangement), they should do so.

7.33 As our recommendations in this chapter are designed to mitigate the impact on individuals, they apply to employers only when the liabilities arises on employees or directors because a company is dissolved or unable to pay the Loan Charge.

Section D: The future

The Loan Charge was intended to shut down loan schemes, but the Review found there were more first-time users in 2017-18 (over 6,000) than in any year dating back to 1999-2000.

Scheme usage continues to be extensive in the 2019-20 tax year to date, with over 8,000 individuals having entered into loan schemes between April and October 2019. A key driver of ongoing scheme usage is a limited number of promoters and professional advisers who are selling schemes in spite of knowing that they will not deliver the tax benefits being promised.

This section of the report summarises some of the wider lessons that should be drawn when designing any future policy in this area, given the ongoing need for the government to do more to combat loan schemes.

Chapter 8

Promoters, advisers, and salespersons

8.1 A very significant number of the individual impact statements spoke of how professional advisers or promoters had convinced people to use loan schemes.

The role of promoters

8.2 The Review received testimony of the sales tactics that would be used by promoters and others to push use of the schemes.

8.3 The tactics they used included misrepresenting the DOTAS system to claim that schemes had been approved by HMRC, or providing opinions from Queen's Counsel (QCs) suggesting that HMRC would not be successful if they tried to claim the tax.

8.4 The Review also received extensive evidence that some advisers minimised the importance of HMRC opening enquiries by suggesting that this was normal. Scheme users therefore felt confident in continuing to use the schemes though they might otherwise have chosen to stop doing so if they had realised the real implications.

8.5 As a result of these kinds of tactics, many individuals and employers who used schemes placed significant reliance on advice of this type in determining whether schemes were legitimate. Taxpayers often placed significant trust in their promoter or advisers because the tax system was not their area of expertise but should have been the professional's.

8.6 The Review also heard that promoters, salespersons, and others continued to push the schemes after December 2010, typically without making the new legal position clear. This directly contradicts respected professional opinion that loan schemes from that point onwards were unlikely to achieve their aims of avoiding tax.

8.7 The Review found numerous examples of contemporaneous promotional material from scheme promoters into the 2010s minimising the risks of using schemes and continuing to present such behaviour as legitimate tax planning despite the clear risks.

8.8 Whilst doing this, some promoters also took considerable fees whilst convincing others to use schemes that they would have known were very unlikely to work.

8.9 Evidence received included worked examples of how scheme users employed through umbrella companies received limited financial benefit from using schemes relative to being employed through a PSC, once promoter and administrative fees were taken into account. It is not possible for the Review to assess how many scheme users will have seen such limited financial benefit, but the temporary tax savings experienced by scheme users will, in some cases, have been largely redirected towards promoters and other professional advisers.

Action against promoters

8.10 Whilst the Review has set out its position that responsibility for tax affairs must ultimately rest with the individual, it is to be expected that people will want expert advice on their tax affairs, and will turn to professionals for that advice. The Review considers that the continuing marketing of loan schemes on the basis of tax benefits associated with them, given the clear legal position, is reprehensible.

8.11 It is also deeply regrettable that the state of the market in tax advice is such that a large number of people were seemingly misled, and many continued to use schemes after 2010 even though the legal position had been made clear. The Review received evidence that certain individuals who were sold schemes have received legal advice that they would stand a reasonable chance of success in litigation against advisors who continued recommending schemes, but for the fact that they are now time-barred from bringing such a claim.

8.12 In a positive move, we note that HMRC has changed elements of its investigative approach to reflect the move to mass market schemes.

8.13 Since 2014, HMRC has moved away from relying on promoters or advisers as intermediaries, thus reducing the risk that they can manipulate information being relayed to individuals. The Review particularly commends HMRC for its new approach of using Real Time Information to determine those who may be using tax avoidance schemes, and then communicating with those individuals before they build large tax liabilities.

8.14 The Review also notes the improvements that HMRC has made to the DOTAS scheme, and the introduction in 2014 of a Promoters of Tax Avoidance Schemes (POTAS) approach which gives HMRC increased powers to pursue a small number of persistent promoters who are not providing the necessary information to enable HMRC to identify those who have used tax avoidance schemes.

8.15 HMRC reported that their activity is now concentrated on the remaining promoters who are likely responsible for the majority of loan schemes presently being sold. In 2019-20, HMRC expect to double the resources involved in tackling promoters.

8.16 In spite of this increased resource, it remains challenging for HMRC to combat promoters of tax avoidance schemes. The evidence from HMRC is that the typical profile of a scheme user has changed towards a higher volume of less affluent users. The marketing of loan schemes has changed to reflect this, and increasingly now imitates legitimate price comparison tools. Promoters now increasingly claim to be offshore, and so are more challenging for HMRC and other UK authorities to enforce against.

Recommendation

8.17 The government must improve the market in tax advice and tackle the people who continue to promote the use of loan schemes, including by clarifying how taxpayers can challenge promoters and advisers that may be misselling loan schemes. The government should publish a new strategy within 6 months, addressing how the government will establish a more effective system of oversight, which may include formal regulation, for tax advisers.

Chapter 9

Tackling the use of loan schemes in future

9.1 The Review received evidence from HMRC that, despite the Loan Charge, schemes continue to be used in significant numbers. There were more first-time users in 2017-18 (over 6,000) than in any earlier year, and there were still approximately 3,000 first time users in the first half of the 2019-20 tax year.[1] The Review also heard convincing accounts of salespersons continuing to publicise loan schemes and pushing other schemes that they claim get around the Loan Charge, which may go some way to explain why they continue to be used.

9.2 Many of the conditions which created a mass market for the schemes also still exist. A large amount of the workforce will be looking for ways to contract their services, with self-employment at 15% of the overall workforce. New ways of contracting and working – the 'gig economy' – may also create a further pool of people to whom schemes could be easily marketed.[2]

9.3 This chapter sets out the future challenges for the government's policies aimed at reducing the use of loan schemes. It notes that the government is likely to return to the area and the lessons that should be learnt from the Loan Charge. Successfully applying these lessons to prevent taxpayers from entering into loan schemes will benefit both HMRC and taxpayers, given the legal position that schemes will not deliver the tax benefits which they purport to achieve.

The government will need to act again to combat loan schemes

9.4 As set out earlier in the report, the 2011 legislation made the legal position of the schemes clear and had a significant impact on the usage of schemes by large corporates.

9.5 The government has also made significant changes that will improve the contracting market. The anticipated changes to IR35 in 2020 will, if implemented, put the onus on larger primary engagers to decide if the off-payroll working rules apply and help to change the balance of power in the relationships between contractors and their engagers.

9.6 There are a number of benefits from the flexibility of the UK's labour market, but as the Taylor Review noted an imbalance of power between employers and individuals, where it exists, can lead to too much risk being transferred

1 HMRC response to request from Review

2 'Trends in self-employment in the UK', Office of National Statistics, 2018

and poorer outcomes for those individuals, such as lower pay and benefits, and imposed employment models including self-employment. Changes such as those in the Good Work Plan published by the Department for Business, Energy and Industrial Strategy aimed at increasing transparency and tackling one-sided flexibility, demonstrate some of the steps being taken to tackle these issues.[3]

9.7 However, the government's objective in introducing the Loan Charge – namely, shutting down the use of the schemes –has not been met. The wider focus on reducing the tax gap, and reducing tax avoidance, is also unlikely to change:

- HMRC estimated the tax gap to be £35bn, 5.6% of tax liabilities, in 2017-18[4]
- there likely remains strong public support for acting against tax avoidance
- the four largest political parties all set out ambitions to reduce tax avoidance in some form in their recent General Election manifestos

9.8 The Loan Charge only applies to scheme usage up until the end of the 2018-19 tax year, and therefore due to the reported continued promotion of loan schemes now, we recommend that the government consider how it will act to reduce their ongoing use, given the evidence that schemes are still being used.

Recommendations

9.9 The Review concludes by setting out the following lessons which are particularly relevant for any future policy aiming to reduce the mass market use of loan schemes.

9.10 Evidence shows that usage of loan schemes continues. Given the Loan Charge was intended as a one-off event, **government should explain how it intends to tackle loan scheme usage in the future**.

9.11 the **strategy for communicating what is considered tax avoidance must be improved** to reflect the mass market nature of schemes.

- HMRC's communications to taxpayers in general should use either mass or, at the other end of the spectrum, direct communications as it is right to no longer rely on promoters or others to pass on accurate information as they have too strong an incentive to obscure the risks of using loan schemes absent much tougher regulation
- In particular, **HMRC should continue enhancing its use of Real Time Information to communicate with taxpayers** who they suspect may be engaging in tax avoidance, and proactively put taxpayers directly on notice of its view

3 'Good work plan', Department of Business, Energy and Industrial Strategy, 2018

4 'Measuring the tax gaps 2019 edition: Tax gap estimates for 2017-18', HM Revenue and Customs, 2019

9.12 The Review received evidence that it was unlikely that loan users were the only ones to benefit financially from the schemes, to the extent that they did. **The Review supports making primary engagers more responsible for the tax status of those they engage and in some cases effectively employ, alongside taking more action against those who promoted the scheme**s (as covered in an earlier chapter). This would better fulfil the original intent behind IR35, while reducing certain of the factors which contributed to the proliferation of scheme usage in the 2000s and early 2010s.

9.13 The Review frequently heard that the government's published impact assessment of the Loan Charge did not take full account of the impact that it would have on individuals and their families. To address this, the Review **recommends that future published government impact notes of tax changes should take proper account of the direct impact on the affected population**. These assessments should also explicitly include interactions between different taxes.

9.14 The Review notes that campaigns on taxpayer issues such as the Loan Charge are likely to be a feature of debates in tax policy in future. **HMRC should learn from the Loan Charge to better respond to such campaigns and communicate more effectively.**

Annex A
Terms of Reference

A.1 The Terms of Reference for the Review were published online on the 11th September 2019. They are reproduced in full here.

Introduction

A.2 The Chancellor has commissioned an independent review of the Disguised Remuneration Loan Charge (hereon 'Loan Charge').

A.3 The Loan Charge is a policy designed to tackle contrived tax avoidance schemes where a person's income is paid as a loan and not repaid. The government is clear that these schemes do not work, that wages paid in this way have always been taxable, and that the underlying tax avoidance behaviour is unfair to the 99.8 percent of taxpayers who did not use these schemes. The Loan Charge was introduced following 20 years of action against these schemes, which despite considerable action continued to proliferate and be used.

A.4 However, the government recognises that concerns have been raised about the Loan Charge policy as a mechanism for drawing a line under these schemes, including claims that the policy is retrospective; the government is therefore commissioning this independent review to consider the impact of the Loan Charge on individuals who have directly entered into disguised remuneration schemes.

A.5 While the Review is ongoing, the Loan Charge remains in force, in line with current legislation; the government will consider the outcome of the Review once concluded and will respond in due course.

Scope and Objectives

A.6 The Reviewer, with the support of a secretariat, is being asked to draw on the available evidence and their expertise, engaging as appropriate with stakeholders, to consider:

- whether the Loan Charge, as it applies to individuals who have directly entered into disguised remuneration schemes, is an appropriate response to the tax avoidance behaviour in question
- whether changes announced by the government in advance of, and since, the Loan Charge came into effect address any legitimate concerns that have been raised about the impact on individuals, including affordability for those affected

A.7 The Review is focused on the impact of the Loan Charge on individuals who have directly entered into disguised remuneration schemes.

A.8 In considering its recommendations, the Review must also take account of:

- the impact on wider taxpayer fairness
- HMRC's ability to tackle tax avoidance effectively in the future

Timing and Recommendations

A.9 The Review will report and provide independent recommendations to the Chancellor of the Exchequer and the Financial Secretary to the Treasury by mid-November.

A.10 The Review's conclusions will be published in a report. The timing and manner of the publication will be determined by the Chancellor of the Exchequer; the Reviewer is expected to use their discretion and will have the final say on the content of the report.

Annex

A.11 Appointment of the lead reviewer: the Reviewer will be appointed by the Chancellor of the Exchequer.

A.12 Resource: they will be supported by a team of officials, drawn from HM Treasury (HMT) and Her Majesty's Revenue and Customs (HMRC). The number of people working on the Review, and the amount of their time spent, will be agreed between the Director of Personal Tax, HM Treasury, and the Reviewer prior to the start of the Review.

A.13 Information: HMT and HMRC must make all possible efforts to support the Review team's work, including providing them with any information that they request, unless there is a legal reason why they cannot do so, which must be detailed to the team. If there is an administrative reason why it is not possible – such as the disproportionate time required to produce the information – then the Reviewer has the right to raise this issue to the Director Personal Tax, HM Treasury, who then can then make a final decision, following consultation with HMRC.

A.14 Governance:

- The Reviewer has the final say on what is published in the report
- It will be for the Reviewer to decide what arrangements are needed to engage with stakeholders during the Review

Annex B
Stakeholders consulted

B.1 As set out in Annex D, the Review requested information to ensure the public were able to share their personal views on the Loan Charge. The Review also requested extensive factual information and documents directly from HMT and HMRC.

B.2 Over 700 personal testimonies, provided via email and through the LCAG, were reviewed alongside submissions by 37 tax and legal experts.

B.3 The Reviewer also met a number of stakeholders. They either requested a meeting with the Reviewer or were selected as an important contributor to the debate on the Loan Charge. Unfortunately, it was not possible for the Reviewer to meet all those who requested a meeting. However, all those that did so were invited to submit written evidence.

Table B.1: List of stakeholders met with

Type	Name
A - Campaign groups and those directly affected	Loan Charge Action Group (LCAG), including meeting with those directly affected by the Loan Charge
B – Government departments and ministers	HM Revenue and Customs (HMRC)
	HM Treasury (HMT), and the Financial Secretary to the Treasury
C – Representative bodies	Association of Independent Professionals and the Self-Employed (IPSE)
	Association of Professional Staffing Companies (APSCo)
	Institute of Chartered Accountants in England and Wales (ICAEW)
	Chartered Institute of Taxation (CIOT)
	Federation of Small Businesses (FSB)
	Low Income Taxes Reform Group (LITRG)
	TaxAid
D- Tax advisers and legal experts	Gordon Berry - Business Oxygen Limited
	Keith Gordon - Temple Tax Chambers
	Matt Hall - Saleos Consultancy
	Phil Manley – PMTC

	Ray McCann - Joseph Hage Aaronson LLP
	Chris O'Hara – Harts Accountants
	Graham Webber - WTT Consulting
D - Members of Parliament and parliamentary bodies	Members of the All-Party Parliamentary Loan Charge Group (Loan Charge APPG)
	Mary Creagh MP
	Rt Hon David Davis MP
	Peter Dowd MP
	Rt Hon Iain Duncan Smith MP
	Rt Hon Dame Cheryl Gillan MP
	Rt Hon Mel Stride MP

Annex C
Investigative approach

C.1 This report considers the impact of the Loan Charge in light of concerns raised by campaigners, Parliamentarians, tax, and legal experts. It considers both the design of the Loan Charge and the approach HMRC have taken to associated compliance and debt collection activities.

C.2 As stated in the Terms of Reference, reproduced at Annex A, the Review is focussed on two key areas:

- whether the Loan Charge, as it applies to individuals who have directly entered into disguised remuneration schemes, is an appropriate response to the tax avoidance behaviour in question
- whether changes announced by the government in advance of, and since, the Loan Charge came into effect address any legitimate concerns that have been raised about the impact on individuals, including affordability for those affected

C.3 The Terms of Reference give the Reviewer final say in what is published in this report. Therefore, while the Review has focussed on the considerations above, it has gone beyond these questions in some areas, where this was deemed appropriate and necessary by the Reviewer.

C.4 The investigative approach is summarised below. The evidence base is described in Annex D.

The Review team

C.5 The Reviewer was supported by a full time secretariat which provided technical, administrative and practical input into the work of the Review to ensure that the timeframe set out in the terms of reference was met. The team was made up five officials from HMT and two officials from HMRC. Other specialist support was drawn in from across government where it was deemed to be of value to the Review, including advice from the Government Legal Department, and from GIAA.

C.6 The Review engaged independent tax and legal advisers, to provide an expert perspective on the Review and its recommendations. They met with the Reviewer on multiple occasions to discuss their views on the Loan Charge and proposed recommendations. These experts also had sight of and provided comments on advance drafts of this report. A range of individuals were considered to support the Review and any potential conflicts of interests were accounted for as part of that process. The Reviewer is grateful to Heather Self, Graeme Nuttall OBE, and David Goldberg QC for providing their expertise and assisting the Review.

The investigative approach of the Review

The objective of the government

Despite a variety of actions to challenge loan schemes the government continued to see evidence of their use in 2016 so considered how to tackle them and prevent use in future. The government decided that the Loan Charge was the most appropriate option.

How this will be achieved

The Loan Charge applies to the outstanding balance of loans paid through loan schemes since 6th April 1999 at 5th April 2019. The balance is taxed as income or trade profits in the tax year 2018-19.

The Review

The Chancellor of the Exchequer commissioned this review to consider the policy impact of the Loan Charge and develop recommendations on how to address any adverse impacts.

Evaluative criteria

Whether the Loan Charge is a proportionate response to the use of loan schemes, specifically whether its design overrides the rule of law and is justified in the context of this type of avoidance.

Whether the Loan Charge is appropriate and affordable for those it affects given their current circumstances.

Other considerations

In considering recommendations the Review has also been asked to take account of:

- The impact on wider taxpayer fairness, including the revenue which be lost as a result of any changes
- HMRC's ability to tackle tax avoidance effectively in future

Evidence base

In summary, the Review considered information including:

- Government published documents, HMRC management information provided to the review and documents such as Office of Budget Responsibility costings
- Reports and other work completed previously by stakeholders such as LCAG and the Loan Charge APPG
- Parliamentary reports and debates
- Over 700 personal testimonies and contributions from 37 tax and legal experts
- Evidence provided in meetings following external consultation with stakeholders

Annex D

Evidence base

D.1 This report's conclusions and recommendations were reached following detailed analysis of evidence collected between September and December 2019 and provided to the Review following a public request for information. The investigative approach is set out in Annex C.

D.2 A wide range, and many different types, of evidence were submitted to the Review. These were considered in their totality to inform the Review's recommendations, and the Review's conclusions regarding the Loan Charge.

D.3 There is a range of work already in the public domain about the Loan Charge which was considered, including:

- the government's report, 'Section 95 of the Finance Act 2019: report on time limits and the charge on disguised remuneration loans', and numerous ministerial statements
- HMT and HMRC statements and guidance
- the LCAG's work, including press releases and correspondence
- the Loan Charge APPG's Inquiry Reports, Survey Reports and documents published on HMRC's conduct
- the EAC's report, 'The Powers of HMRC: Treating Taxpayers Fairly'

D.4 The Review considered the history and development of loan schemes since 1999, including the effectiveness of HMRC's approach to challenging them before the introduction of the Loan Charge.

- HMRC management information and narrative explanations were requested and analysed, which was compared against information and data from other sources
- wider trends were also considered by reviewing work completed previously on changes in the labour market, such as the Taylor Review
- the Review carried out external consultation with a range of groups with relevant experience, including tax advisers, accountancy firms, professional bodies, and lawyers
- the Review considered the personal testimonies of those who had used loan schemes, as provided through emails directly to the Review and by the LCAG

D.5 The Review sought to understand the legal position of the Loan Charge and of loan schemes over time, including the impact of tribunal and court rulings.

- the Review considered how tax law had developed through legislative change and court decisions relating to loan schemes. This included reviewing contemporaneous debates on legislation, government consultations, and their responses

- the Review compared the interpretations provided by HMRC and the legal and tax professionals consulted. It also considered the expert commentary which has been published on the issue

- the Review formally engaged independent legal counsel in David Goldberg QC

D.6 The Review considered experiences of those affected by the Loan Charge, their financial position, and the impact of measures announced by the government to address the concerns raised.

- HMRC management information and narrative explanations were requested and analysed, which was compared against information and data from other sources such as the Loan Charge APPG's Inquiry and linked surveys

- the Review met with those directly affected through the LCAG. The Review also met with a number of MPs from all major parties, who shared their constituents' experiences

- the Review considered the personal testimonies of those who had used loan schemes

D.7 The Review sought to understand the financial position of taxpayers facing the Loan Charge. Comprehensive data on what all of those facing the Loan Charge owe, and have in income and assets, was not available, so the Review explored what could be inferred from the existing data.

- the Review requested, and was provided, data on the distribution of income of those facing the Loan Charge who had already settled, and those who had not already settled from HMRC

- the Review requested, and was provided, anonymised data on individuals that had settled the Loan Charge where their income was known from either Self Assessment or PAYE – this enabled the comparison of individuals' income to the amount they owed

- the Review requested data on the assets of those facing the Loan Charge, which was not available as HMRC do not systematically record data on individuals' assets

- the Review looked at statistics from the ONS Wealth and Assets Survey, and the Bank of England/NMG Household Survey to understand what assets the average household in an income bracket would have

- the Review was unable to assess how similar those facing the Loan Charge are to the general population in terms of the assets they have, so the Review has not relied on these statistics in the final report

D.8 Where necessary the Review undertook background research to understand the context around the use of loan schemes and the Loan Charge. This includes, but is not limited to, general principles in the tax system, the history and development of mass marketed tax avoidance, and labour market changes over time.

D.9 The Review considered the recommendations which it feels can address the issues identified. The Review assessed the potential impact of these measures on scheme users if they were implemented by the government, drawing on the evidence available to it.

Request for information

D.10 To ensure the widest range of evidence was available and that the public were able to share their personal views, a request for information was published on 17th September 2019.

D.11 The request was published on gov.uk and shared by others such as LITRG and Contractor UK. The request invited submissions via email by 30th September 2019.

D.12 Over 700 personal testimonies, provided via email and through the LCAG, were reviewed alongside submissions from 37 tax and legal experts.

D.13 The Review considers the confidentiality of taxpayers to be of the upmost importance and took steps to ensure this was preserved:

- HMRC did not provide any information with which the Review could identify individual taxpayers

- no evidence received by the Review was shared with HMRC or HMT

- no information which would be used to identify individual taxpayers was shared with HMRC or HMT

D.14 HMRC offered the Review the opportunity to corroborate evidence received from taxpayers against information they hold. The Review decided not to accept this offer to preserve the confidentiality of those who provided information.

D.15 All evidence received by the Review will be destroyed at its conclusion and those that provided evidence were informed of this at the time.

Annex E

Technical explanation of how the Loan Charge works

Legislation

E.1 The Loan Charge builds on legislation at Part 7A, Income Tax (Earnings and Pensions) Act 2003 (employment income provided through third parties) (ITEPA) and usually described as the 'disguised remuneration' provisions. Part 7A was introduced by Finance Act 2011 and is referred to in this report as 'the 2011 legislation'.

E.2 In imposes an employment income charge, in the hands of the employer under PAYE, broadly where each of the following conditions are met:

- there are arrangements provided for employees
- a third party, being any other person than the employer unless the employer is acting as trustee, takes a 'relevant step' – which would include making a loan
- it is reasonable to suppose that the relevant step is taken pursuant to the arrangements for employees

E.3 The Loan Charge was announced in 2016. Legislation was introduced in Finance Acts (No. 2) 2017 and 2018.

E.4 The Loan Charge applies to loans made through loan schemes on or after 6th April 1999 and which are still outstanding at 5th April 2019, treating a person as making a relevant step at that date. This creates an employment income charge in the 2018-19 tax year where the other conditions in the 2011 legislation are met.

E.5 The legislation includes a number of reliefs which attempt to ensure there is no double taxation. Notably, where there is an overlap between the 2011 legislation and another income tax charge.

E.6 There are matching provisions in Income Tax (Trading and Other Income) Act 2005 (ITTOIA) which apply where individuals using loan schemes that provide their services without an employment relationship.

Transfer of liability

E.7 The liability to pay the income tax on the Loan Charge rests with individuals. However, the obligation to operate PAYE to collect it arises on the employer.

In some cases, HMRC transfer the liability to the individual, either automatically as set out in legislation or using a direction.

E.8 HMRC's stated approach, for both the Loan Charge and underlying liabilities, is to seek the tax from the employer in the first instance. Where the employer meets an individual's liability it is a common law principle that it can recover the money from the employee.

E.9 HMRC consider transferring the liability to the employee where the employer is unable to pay. They can do so in certain circumstances under the Income Tax (Pay As You Earn) Regulations 2003. Where the employer no longer exists, the Loan Charge liability automatically rests with the individual.

E.10 Around 80% of individuals who have used a loan scheme involved an employer in an offshore jurisdiction. Normal rules would transfer the responsibility to operate PAYE to the first onshore party involved in supplying an individual's services. The Loan Charge legislation 'switches off' this rule, as HMRC consider that the onshore entity would not have benefited from the use of the loan scheme given the frequency with which offshore entities are involved and the onshore entity would have no power to establish the outstanding loan balance.

Annex F
Glossary

Term	Definition
Accelerated Payment Notice (APN)	Introduced in Finance Act 2014, as part of a package of measures to change the economics of avoidance. APNs allow HMRC to collect amounts of tax and NICs under dispute as a result of the use of a tax avoidance scheme, including but not limited to loan schemes. When an APN is issued scheme users must pay the amount of tax and NICs specified by HMRC within 90 days.
Agency, often referred to as intermediaries.	Agencies are generally recruiters who look to supply engagers with flexible labour. There are often several agencies in the supply chain between the engager and the individual providing their labour.
Contractor	Individual providing flexible professional services to an engager, either directly or through an agency. Typically considers that they are self-employed and sometimes offer their labour through a PSC.
Disclosure of Tax Avoidance Schemes (DOTAS)	Introduced at Part 7 Finance Act 2004 for HMRC to obtain early information about how tax arrangements work and information about who has used them. Disclosure has no effect on the underlying tax position of a taxpayer or tax avoidance scheme, but there may be penalties for failure to disclose on both the promoters and scheme users.
Discovery Assessment	Discovery Assessments allow HMRC to prevent "any loss of tax" by assessing a person for the amount that should have been paid.
Engager	Organisations seeking flexible labour to meet a specific need without wishing to employ individuals themselves. Generally contract with an agency/intermediary to provide them with this labour. They are the 'end-user' of an individual's services.
Enquiry	May also be referred to as a compliance check. It is the process by which HMRC check in detail that the information on a tax return is correct and complete.
Follower Notices	Follower Notices can be issued to scheme users of a scheme that has been shown in another litigation case to be ineffective. The follower notice tells the scheme user that they may be liable to a penalty of up to 50% of the disputed tax and/or NICs if they choose not to settle with HMRC at that point and are later defeated in court.

HM Revenue and Customs (HMRC)	HMRC is the UK's tax, payments and customs authority.
Loan Schemes	Defined by the government as Disguised Remuneration (DR) schemes, a wider category of employment tax avoidance. Arrangements through which individuals are rewarded through a third party in the form of loans, usually involving an offshore trust. Outstanding balances on these loans at 5th April 2019 are subject to the Loan Charge in the 2018-19 tax year.
Off-payroll working rules (IR35)	Taking effect from April 2000, off-payroll working rules apply if a worker provides their services though an intermediary. The rules make sure that workers, who would have been an employee if they were providing their services directly to the client, pay broadly the same tax and NICs as employees.
Personal Service Company	Limited company that typically has a sole director, usually a contractor, who owns most or all of the shares. Provides the professional services of that contractor to an engager, either directly or through an agency.
Promoter	Those who devise and market the use of loan schemes. Including securing QC opinions, producing promotional material and marketing the schemes, either to agencies as an option for their staff or directly to contractors. Can be summarised as anyone who in the course of providing tax services: • is to any extent responsible for the design of a tax scheme (defined by reference to DOTAS) • approaches others with a view to making a scheme available to them • makes a scheme available for implementation to others • organises or manages the implementation of a scheme
Protected Year	A year where HMRC has protected its position by opening an Enquiry within set time limits, has a valid Discovery Assessment in place or is still in time to do so. HMRC's position is that amounts from these years would be collected through its compliance and litigation activity, without the Loan Charge.
Self Assessment	Self Assessment is a system HMRC uses to collect Income Tax where it is not collected through PAYE. Completed for each tax year, ending 5th April, and due (online) on 31st January following the end of the tax year.
Scheme Reference Number (SRN)	Issued to the promoters and co-promoters of any DOTAS registered scheme. They must send on to their clients and further clients until the final user has received it. Uses of DOTAS registered tax avoidance schemes must include the SRN on their return.
Tax Avoidance	According to HMRC's online guidance tax avoidance involves bending the rules of the tax system to gain a tax advantage that Parliament never intended. It often involves contrived, artificial transactions that serve little or no purpose other than to produce this advantage. It involves operating within the letter, but not the spirit, of the law.

Tax Evasion	Tax evasion is where there is a deliberate attempt not to pay the tax which is due. It is illegal.
Tax Planning	Tax planning is the analysis of a situation and structuring of affairs in such a way to ensure tax efficiency. It involves reviewing the various opportunities and relief available within legislation to ensure that tax bills are minimised.
Tax Year	For individuals the Self Assessment tax year starts on the 6th April and ends 5th April the following year, for example the 2018-19 tax year began on 6th April 2018 and ended on the 5th April 2019. For corporate bodies the tax year depends on the end of the accounting period.
Umbrella Company	An umbrella company is a UK limited company which acts as an employer to a number of individuals, meeting PAYE and other requirements where operating legitimately. It signs contracts to provide the individual's labour to engagers, either directly or through another intermediary such as a recruitment agency.
Underlying Liabilities	Tax due from loan scheme use in earlier year, including late payment interest and other amounts such as inheritance tax. HMRC consider that these amounts are due irrespective of the Loan Charge, though it may need to bring litigation to prove that this is the case.
Unprotected Year	A return period where HMRC has not opened a valid Enquiry within time limits and does not have a valid Discovery Assessment in place. Unless extended time limits apply HMRC would be out of time to collect amounts they consider due as a result of loan schemes, absent the Loan Charge. Taxpayers were required to pay Voluntary Restitution for these periods under the November 2017 settlement terms to ensure that they are not subject to the Loan Charge.
Voluntary Restitution	Paid, but not technically required, for Unprotected Years as part of the November 2017 settlement terms. Paying Voluntary Restitution for a year will prevent a future charge arising, specifically the Loan Charge. Calculated at rates and bands applicable in the year the loan scheme was used. Once agreed with HMRC in the form of a settlement contract, it becomes legally enforceable. Failure to pay Voluntary Restitution will result in the Loan Charge arising in respect of Unprotected Years.

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