HMRC attack on EBT loans

Nigel Holmes
Armstrong Watson
Nigel Holmes is a partner at Armstrong Watson. He specialises in tax planning for companies, and his specialist areas include remuneration planning, employee benefit trusts, research and development tax relief, reorganisations and planning with shares and capital allowances. Email: nigel.holmes@armstrongwatson.co.uk; tel: 01228 690200.

The recent Budget contained references to disguised remuneration. Has HMRC arranged for its plans to be contained with the 2011 tax changes? What are the details to accompany the chancellor's references? And, surely, these changes will not impact EBTs which predate the 2011 rules?

The chancellor did indeed refer to disguised remuneration in his Budget speech of 16 March. The detail, if you can call it that, was to be found in a technical note, which can be found at www.bit.ly/1VQOmVm.

The forthcoming changes will affect anyone with outstanding loans from employee benefit trusts (EBTs) and similar trusts, and those who have received loans under a contractor loan scheme. In short, the technical note refers to a future income tax and national insurance charge, by way of an amendment to ITEPA 2003 Part 7A, which will apply to all loans still outstanding on 5 April 2019 that have not been repaid or taxed in full by reaching an agreement prior to this date with HMRC.

The document also seeks to further strengthen anti-avoidance measures to prevent promoters and advisers looking for ways to circumvent the Part 7A charges.

The disguised remuneration legislation was introduced in Finance Act 2011 and came into effect from the date it was announced on 9 December 2010. The HMRC guidance that accompanied Part 7A made it clear that loans in place as at 9 December 2010 were not caught by the disguised remuneration legislation; instead, they were taxable by applying existing principles, namely as employment loans giving rise to a benefit in kind tax charge.

What do we know so far? Firstly, the technical note contains very little detail. There is reference to a consultation which is due to take place in the summer, and confirmation the legislation will appear in Finance Bill 2017 and that a new tax charge will arise within Part 7A.

However, there is further information about HMRC's intentions in one of its technical briefing webinars.

HMRC considers the interim period between now and 5 April 2019 to be a 'period of grace', which should give affected taxpayers the time to extract themselves from tax avoidance schemes and to bring their affairs in order. The options are:

- repay the loan (this ties the funds back up in the trust with tax consequences if the taxpayer extracts them again, and cash flow issues); or
- reach an agreement to pay tax.

There are no specific inducements to taxpayers to extract themselves from any affected schemes. There is merely a suggestion that the amount they pay may be less than the charge that will be due on 5 April 2019.

A Part 7A charge, as earnings, will be levied on the loan or loans outstanding. A tax charge will also be calculated on the loan at the time it was made, and interest calculated thereon. The former charge will be deducted from the latter and, if a balance is due, then the tax will be both the 5 April 2019 charge and the balance. Could it have been made any more complicated?

Particular points

What happens if HMRC has already investigated your EBT? In this situation, you might have thought that you would be unaffected; however, this is not the case, according to HMRC's webinar. This suggested that the legislation will apply to all loans, including both those loans which HMRC was aware of but where it had not taken action, and those periods that are out of time for enquiry.

Not only is this retrospective but it is likely to cause significant unrest among the tax advising community. In particular, it will cause financial damage to taxpayers, some of whom may face bankruptcy.

What happens if the client has paid tax by way of a benefit in kind. When that is offset, will the charge will be manageable? Although you may have thought so, this will not be the case. Despite HMRC's suggestion that there will be no double charge to taxation, no offset will apply to the 5 April 2019 charge. By settling now, however, you *may* be able to negotiate this.

If this is the incentive to settle, a more robust offering with some clear parameters would be welcome.

What happens if the employer has been liquidated? If the employer was liquidated many years ago, your client may wrongly consider that they will be unaffected. The charge will be levied on the employer in the first instance; however, where this is not possible, the charge will be levied on the employee. There are questions about whether this will include employer's national insurance. There are also uncertainties about how this will impact documentation and assessment.

How will HMRC know that there are EBT loans? Good question. Many of those loans known as 'vanilla' EBTs, or 'EBT-lites', are not under enquiry and HMRC will have very little knowledge of them. However, HMRC's position is that failure to come forward by 5 April 2019 will turn an avoidance issue into an evasion issue.

What else should I know?

Currently, a loan of this type can be written off without tax charge on death. Whilst no one wants to use their own death as a tax planning mechanism, for those with a terminal illness it may be worth doing nothing for now.

Where the employer still exists, the draft legislation will consider the interaction with other taxes, such as corporation tax relief. Wouldn't it be great if this relief was deducted from the charge on the employee, if the employer no longer existed? This, however, is highly unlikely.

There is no mention so far of inheritance tax. Exit charges can arise from such trust transactions; and while there are usually reliefs available to avoid double taxation, HMRC did seek the double tax charge in some cases under the EBT settlement opportunity that recently closed.

There is no consideration to trust law and trustee responsibilities when forcing these tax charges on trust transactions.

What should you do now?

Most taxpayers and advisers will, I am sure, await the detail which will be released following the consultation.

Taxpayers affected by these proposals should seek to collate their information, speaking to their trustees where necessary, and seek advice now in anticipation of the consultation.

Advisers should respond to this consultation. Retrospective taxation and taxing transactions that have previously been considered by HMRC is, in my opinion, a step too far.

We await the consultation with a mixture of anticipation and dread. ■