Written evidence submitted by John Clarke (FB18)

The Finance Bill and Contractor Loans

The punitive impact of the Loan Charge contained within this bill should address a number of issues:

- Doesn't impact promoters as the government won't or can't pursue a retrospective law
- It glosses over HMRC's failings and allows them to continue
- End users have 20 years of loans calculated as if they were income in a single tax year
- Blackstone's Theory: Many individuals who used loan arrangements have not even been contacted by HMRC and will therefore not be impacted, whilst those who have been fully transparent with their tax affairs will be ruined by the Loan Charge.
- Otherwise thriving small businesses with many employees, driven into insolvency

The Terms of Reference associated with the Loan Charge review quite understandably poses several questions, but they appear very prescriptive and they oversimplify what is a complex issue that has been allowed to build up over two decades. Conveniently for HMRC/HMT the questions pre-conceive the notion that it was a tax avoidance motive that was the primary driver for why contractors and small businesses entered into these arrangements. The reality is very different, and HMRC/HMT know this full well. Without any doubt it was the individual's endeavour to maintain compliance in the wake of the very poorly drafted and implemented IR35 policy that is at the heart of this, and the subsequent misleading advice from those in positions of authority paved the way for use of these arrangements to proliferate.

Why did people start using loans?

Did 50,000+ people and small businesses really set out 'to aggressively avoid tax' or intentionally enter into an arrangement that they thought was not legitimate? No. They were motivated by anxiety. They were overwhelmed by the sheer volume of information in the tax code and wanted to reduce the risk of becoming embroiled in unnecessary and unwarranted IR35 investigations. So, they followed professional advice and purchased solutions to delegate the responsibility and administrative burden of operating a limited company. There is an assumed degree of financial knowledge on HMT and HMRC's behalf in their rhetoric. The people who signed up range from all walks of life, business people, consultants, nurses, doctors, teachers and many others who are experts in their own professional fields not tax law. Most have no interest in tax law either. They concentrate on undertaking the work they are qualified to do and are good at, and quite understandably engage qualified tax professional to handle matters that concern their tax status. The British tax code is

currently more than 17,000 pages. It has more than trebled in size since 1997. On your own it would be impossible to digest such a glut of information, and yet we are often told that ignorance of the rules is no defence. Clearly there must be a point where it just becomes impossible to keep abreast of the tax code. There is a quantum leap between being a PAYE employee and trying to run a business as a contractor. Working as an employee you can leave almost all tax matters to your employer's payroll department as they will calculate and deduct the relevant tax through PAYE. Running your own business requires being responsible for all your tax affairs. On your own you can fall into a thousand tax traps very easily even whilst engaging qualified tax professionals. Without engaging them you would be virtually helpless. For this very reason those affected did not look to set up their own processes, they would not have had the knowledge. They became customers of established arrangements that were managed by people who were specialists in accountancy and taxation, and who had teams that ensured "ongoing compliance" was provided for users which in turn gave "peace of mind." Those arrangements were mass marketed and promoted by big companies over many years. The assertion that arrangement users were out to "beat the system" is risible. They were out to work as best they could and comply with the law in the simplest way possible. LCAG Briefing Document to the Loan Charge Review Page 7 of 20 Treasury and HMRC have continually sought to demonise users of these arrangement and misrepresent the reality of the situation as well as people's intent. These HMRC tactics have directly led to the mental breakdown of thousands and regrettably six suicides have been directly attributable (and evidenced) to the Loan Charge and the behaviour of HMRC/HMT. It has also been extensively reported that there has been widespread degradation in normal healthy family relationships resulting in relationship break-ups for many. This is despite the official HMRC impact assessment, which claimed that the Loan Charge "would have no effect on family stability". When one considers that noone has broken any law, is this fair? Is this justifiable? Is this what parliament intended?!

2.2 HMRC's Knowledge

HMRC have known about these arrangements since the 1990s and did little to challenge them. In fact, they only started to have a problem with them once they had become established in the mainstream and many contractors started to use them, precipitated by the inception of IR35. It took them significantly longer to start challenging them in any meaningful way. Occasionally they took arrangementsthrough the courts but their argument that a loan was income was alwaysrejected. It was acknowledged by a National Audit Office report in 20121 that HMRC needed to do more to tackle these mass marketed arrangements. Meanwhile more and more arrangements were set up and they became commonplace. Loan arrangements became increasingly popular and were rarely challenged, giving an appearance of tacit acceptance by HMRC. HMRC allowed users to carry on using these arrangements for many years and made little or no effort to address their widespread use. The inconsistency of HMRC's actions were also noted, where a taxpayer would use the same arrangement year after year, but enquiries were opened only on some of the years whilst others were successfully signed off and left

unchallenged. There is a distinct and concerning haphazardness and disorganisation to the administration of enquiries during this time. In the cases where enquiries have been opened those were dismissed as routine by both HMRC and accountants. Users were told that HMRC would be in touch if there was any problem. HMRC rarely did. In most cases enquiries have been languishing in the void for many years. Indeed, we have on record that HMRC opened enquiries 13 years ago into an individual's tax returns, and no further communication has ever been received by the individual.

DOTAS

DOTAS (Disclosure of Tax Avoidance Schemes) was envisioned as a means of controlling tax avoidance arrangements and was introduced in 2004. DOTAS numbers were issued to arrangements that bore specific hallmarks. Some arrangements, that have been deemed as subject to the Loan Charge, (legitimately) weren't issued with DOTAS numbers. There were even cases of individuals contacting HMRC at the time to be told that their arrangement was in order and they were not required to declare anything. 1 https://www.nao.org.uk/wp-content/uploads/2012/11/1213730.pdf LCAG Briefing Document to the Loan Charge Review Page 8 of 20 Promoters used DOTAS registration to their advantage by positioning their arrangements as being fully registered and legally compliant. When people were in DOTAS registered arrangements and no action had ever been communicated or taken, what else were they expected to think? Had HMRC been clearer on what a DOTAS number signified, the acceptance of them by contractors may have been severely impacted.

Have HMRC always been clear that the arrangements didn't work?

HMRC repeatedly uses the terms "HMRC believes", "HMRC has a view" or "HMRC's opinion" to justify its actions. It is not HMRC's function to hold opinions, only to apply the tax code. These are classic behavioural insight nudging techniques to coerce people into believing they owe tax when they may not. HMRC should hold itself to a higher standard given the power and influence it already has over taxpayers. HMRC's stated position is that they have always said these arrangements did not work. This raises several crucial questions. • In what way did they communicate this to taxpayers and when? HMRC's Spotlight articles are not read by the people being targeted here – the first mention of contractor loans came from one of these newsletters as late as 2013. Only tax advisors and tax insiders read Spotlight articles. Contractors leave their tax affairs in the hands of these advisors. If the advisor does not pass on that information or make the necessary changes then the contractors will be completely unaware. Equally, whispers within HMRC or speeches given to Commons Committees are not law and certainly do not reach the average taxpayer. DOTAS could be interpreted as a vague attempt but once again its purpose wasn't made clear and it was routinely used to provide credibility to the arrangement rather than to dissuade users from signing up. Despite personal and company tax returns being made to HMRC, and with notices issued by HMRC acknowledging receipt, no communications were made in respect of these

arrangements nor any advisories issued to individuals. • On what basis were they clear arrangements didn't work? The only significant court ruling regarding these arrangements has been the Rangers Case. The final ruling, after all lower courts found against HMRC, was at the Supreme Court in 2017. Unusually, the Supreme Court gave judicial leniency and permitted HMRC to change their argument. The premise HMRC had previously based their objections on were not winning the courts over. So, in what way could HMRC have, "always have been clear", when until 2017 there was no determination made in law. And when indeed the courts did rule, until the final supreme court ruling in 2017, prior to then all HMRC's objections were dismissed by the courts. It would be far more honest and fairer to say that HMRC "did not want them to work." LCAG Briefing Document to the Loan Charge Review Page 9 of 20

Were arrangements really "Too good to be true"?

We have heard the "too good to be true" phrase so often it is beyond cliché. It is also simply wrong if approached from the perspective of someone not well versed in tax. A typical scenario was that an individual checked with the promoter or accountant for re-assurances that the arrangement was legal and legitimate; such as the arrangement having been reviewed by a QC, the promoter would claim that the DOTAS number was HMRC approval etc. This, combined with how widespread they were and the take home being broadly in line with that offered via the limited company option, made the use of loan arrangements appear both reasonable and realistic. Another type of scenario was for agency workers such as nurses and supply teaching staff. They were paid by the agency without even knowing they had entered into such arrangements. Employment agencies managed all their tax affairs, and some were even instructed to use a particular umbrella company as a condition of work. In some cases, avoidance of tax may have been a motive. But in most cases, when compared with the limited company option that would be the contractor's benchmark, there was little difference; and this is one very clear reason why "too good to be true" is a complete smokescreen. Regardless, tax avoidance was, and still is legal and certainly for most of the 20 years covered by the Loan Charge tax avoidance was not the pejorative term it has been conflated into. It was simply described as tax planning or minimising one's tax liability by legal methods (something all legal dictionaries will detail). Fundamentally there is no requirement to pay more than is legally due and a constitutional principle of English law states that, "everything which is not forbidden is allowed". Without the Rule of Law, we have nothing.

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