EdwinCoe LLP

GUIDE

What now for Directors and Advisors following HMRC's successful challenge to EBTs and disguised remuneration schemes?

HMRC's success in the Glasgow Rangers case in 2017 is well documented and follows a political sea-change as a consequence of EBTs having been abused as tax avoidance schemes, often for the purpose of avoiding payment of PAYE and NIC to key employees.

Unsurprisingly this has become increasingly contentious for HMRC which is often the largest creditor in any subsequent insolvency. Increasingly we are seeing HMRC exerting pressure on Insolvency Practitioners to pursue directors personally for operating an abusive EBT, not to mention encouraging liquidators to file adverse reports recommending the commencement of director disqualification proceedings.

Practitioners will be aware that HMRC has led the challenge to disguised remuneration schemes, taking the view that funds paid into these schemes are earnings on which PAYE and NIC were due and which the employer should have accounted for. Concerted efforts have been made to clampdown on their use, including the issuing of accelerated payment notices (APN) when there are arrangements that fall within DOTAS rules. This has been followed by the Finance Act 2018 implementing charges on employers with unpaid tax liabilities arising from disguised remuneration schemes, should these liabilities not be settled by April 2019. Employers can also be held liable for unlimited fines and/or criminal prosecution if the employers have been involved in tax evasion. Future proposals include how HMRC will deal with directors who misuse insolvency for the purpose of avoiding tax.

These, and various other legislative provisions, give rise to two potential claims that Insolvency Practitioners may have against directors. The first is for misfeasance pursuant to Section 212 of the Insolvency Act 1986 (the Act). The second is for transactions defrauding creditors pursuant to Section 423 of the Act.

The misfeasance argument goes as follows. All directors owe a fiduciary duty to act in the best interest of the company and this is breached by participating in tax avoidance schemes which give rise to a loss to creditors, including HMRC. Whilst a director may try and rely upon the advice given by the scheme's introducer (normally backed by a QC's opinion) that may not necessarily apply post 2011 when HMRC first began targeting such schemes (following the Finance Act 2011) and the publicity surrounding the Glasgow Rangers case.

Where a director is found guilty of misfeasance then a Court has very wide sanctions, including ordering a director to contribute to the losses to the creditors.

The argument that paying funds into a tax avoidance scheme is a transaction to defraud creditors is as follows. All directors are aware of their duty to ensure a company pays tax on behalf of itself and its employees.

By paying monies that would otherwise be available to pay such tax for some other purpose - usually disguised remuneration - means monies that should otherwise have been available to pay HMRC have been put out of HMRC's reach. Contrary to its title there is no need for a liquidator to prove fraud. All they have to prove is that the payment was one of several substantial reasons. Moreover Section 423 of the Act allows HMRC to pursue claims directly against directors, without the involvement of the liquidator. Increasingly we are seeing HMRC working hand-in-glove with Insolvency Practitioners by nominating them to become liquidators and then supporting them, sometimes with financial assistance, to pursue directors.

So what defence would a director have in these circumstances? In reality it all depends upon the legal advice they received at the time of entering the scheme and whether in doing so they exercised reasonable care, skill and diligence and/or acted honestly and reasonably.

Weighed against this HMRC will argue that directors are often fully aware of the risks they were taking, particularly given the critical environment within which EBT structures are being challenged. Even relying upon professional advice is sometimes difficult given that the advice normally contains numerous caveats and often will include advice to reserve funds in case a scheme does not work.

There have been various recent cases involving challenges by HMRC and liquidators, often at the prompting of HMRC, and these cases will undoubtedly increase in volume as the political climate of 'austerity versus corporate greed' prevails. We at Edwin Coe have extensive experience of acting with directors facing such claims, as well as their advisors, whom HRMC and Insolvency Practitioners are increasingly considering their role in promoting such schemes. If you or your clients would like advice or assistance then please do not hesitate to contact us.

Our Team

For individual profiles please visit our website: www.edwincoe.com.

If you would like further advice please contact Ali Zaidi – Head of Litigation and Insolvency, or any member of the Restructuring & Insolvency Team.

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