



Response from ICAS

**Tax Abuse and Insolvency:
A Discussion Document**

13 June 2018

About ICAS

1. The Institute of Chartered Accountants of Scotland ('ICAS') is the world's oldest professional body of accountants and we represent over 21,000 members working across the UK and internationally. Our members work in all fields, predominantly across the private and not for profit sectors. ICAS is a Recognised Professional Body (RPB) which regulates insolvency practitioners (IPs) who can take appointments throughout the UK.

General Comments

2. ICAS welcomes the opportunity to respond to the HMRC discussion document 'Tax Abuse and Insolvency' published on 11 April 2018. We support the efforts of the Government to take appropriate steps to deter and deal with abuses of insolvency processes and to minimise the tax gap between what is due to HM Revenue & Customs and what is paid.
3. We were pleased to have the opportunity to meet with HMRC officials dealing with the consultation on 30 May 2018. This response summarises and builds on our comments made during that meeting. We would be pleased to have further discussions with HMRC about any of the matters raised in this response.
4. ICAS is interested in securing that any changes to legislation and procedure are based on a comprehensive review of all the implications - and that alleged failings within the insolvency process are supported by evidence.
5. The discussion document is one of a few consultations and discussion documents issued in recent months by the UK Government which relate to insolvency. We believe that while each of these consider distinct areas, there is a synergy between them and it would be helpful to consider aspects of the different consultations alongside each other. In addition to this discussion document the other consultations are:
 - Insolvency and corporate governance, Department for Business, Energy & Industrial Strategy
 - Extension of the existing security deposit legislation to include CT and CIS deductions, HMRC.
6. Our general comments relate to broad principles around proposals for changes linked to insolvency. We comment below (paragraph 11 onwards) on the specific proposals in this discussion document – which were discussed at our meeting with HMRC on 30 May.
7. The UK has a highly respected insolvency and restructuring regime. It currently ranks 14th in the World Bank Resolving Insolvency Index. The insolvency regime is part of a wider macro economic system for an effective and functioning economy and contributes towards a country's economic growth. It is important to ensure that any future steps affecting the insolvency regime will not unduly harm the UK and hinder economic growth.
8. The Government acknowledges that the vast majority of insolvencies in the UK are for genuine reasons and there appears to be no suggestion that there are widespread issues with the insolvency regime in the UK. We agree with this assessment. Future changes should therefore be targeted at the specific issues identified in the three areas currently under examination. It appears difficult to quantify the extent of the problem or the losses in each of the three areas and therefore to quantify the benefit that might be obtained from the proposed actions.
9. One of the areas identified is phoenixism. While this may be broadly referred to as a concept, in reality it is difficult to define. There is no legal definition in the UK of phoenixism and what is sometimes described as phoenixism could also, in certain circumstances, encompass serial entrepreneurship. Often what is referred to as a phoenix operation will have resulted from a business or asset sale which maximises the return to creditors out of an insolvent situation – the primary responsibility of an insolvency

practitioner. It may also maximise the preservation of employment. A distinction should therefore be made between abusive phoenixism and other forms of phoenixism.

10. The UK promotes entrepreneurialism and a rescue culture for financially distressed businesses. Any proposed actions should therefore take account of the potential detrimental impact of placing limitations on, or barriers to, a rescue environment.

Comments on the measures proposed in the Tax Abuse and Insolvency Discussion Document

11. We do not believe that the measures proposed in this consultation will generally be appropriate to tackle phoenixism because of the risks outlined in our general comments. Removing phoenixism from the scope of these proposals would be a significant step towards ensuring that genuine multiple insolvencies would not be caught by the measures. It would also make it easier to define the criteria to be met before the proposed measures could apply. We believe that extending the security deposit legislation to CT – proposed in the separate consultation “Extension of the existing security deposit legislation to include CT and CIS deductions” – could be used more effectively to target abusive phoenixism.
12. The criteria that would need to be met, in order to fall within the scope of any of the new measures proposed in this consultation, must be well defined. There would be a benefit in aligning these with criteria used in other legislation – which will be well understood.
13. We believe that STAR (Serial Tax Avoidance Regime) would be a useful starting point in identifying appropriate criteria for applying the new rules. This would cover arrangements:
 - counteracted under the [general anti-abuse rule](#) (GAAR)
 - where HMRC has issued a [follower notice](#)
 - which fall under the [disclosure of tax avoidance schemes](#) (DOTAS) rules
 - which are notified or notifiable under the [VAT avoidance disclosure regime rules \(VADR\)](#)
 - fall under the disclosure of tax avoidance schemes for [VAT and other indirect taxes’ \(DASVOIT\) rules.](#)
14. We do not believe that Targeted Anti Avoidance Rules (TAARs) should be included as a trigger to bring cases within the scope of the proposed new measures, as it is possible to fall within a TAAR inadvertently.
15. As an example, the TAAR relating to distributions in liquidations was intended to deter phoenixism. In many solvent liquidations it is unlikely that the avoidance of paying tax debt is the objective, although in some cases the intention may be tax avoidance through repeatedly extracting funds from a series of companies at favourable CGT rates. However, the introduction of the TAAR has caused problems for business owners, insolvency practitioners and advisers in cases where there is no intention to avoid paying tax debt and no tax avoidance motive – because of uncertainty about the application of the TAAR. An individual may genuinely intend to retire from full time work but later decides to do some part time work, in circumstances which could bring them within the TAAR.
16. In addition to the STAR criteria we would also support the use of “deliberate behaviour” as set out in Schedule 24 Finance Act 2007 and Schedule 41 Finance Act 2008 as a trigger for tax evasion to be brought within the scope of new provisions.
17. In addition to those entities which go through a formal insolvency process, a significant number of entities will not go through such a formal process, instead being struck off the Register of Companies either through an application process under the Companies Act 2006 or through action taken by the Registrar as a result of the company failing to submit the required returns. It is likely that those engaged in abusive behaviour will seek to exploit this route to company dissolution. Any measures introduced must therefore

capture entities which are dissolved in this way as well as those in formal insolvency processes.

18. Two possible approaches are set out within section 3.5 of the discussion document - extension of transfer of liability and joint and several liability. We have concerns about the joint and several liability approach, particularly around identifying appropriate safeguards; as discussed at our meeting with HMRC it is hard to see what effective safeguards could be provided in the case of prospective debts. We also have concerns that joint and several liability presents a finance funding risk to business. In certain circumstances this could restrict access to business funding, or adversely affect funding pricing, for genuine businesses, particularly when faced with a business rescue situation. This approach would also introduce a fundamental change to the concept of limited liability status.
19. Transfer of liability would be a more appropriate approach to tackling abusive behaviour. This could be more effectively targeted, and it would be much easier to include appropriate safeguards. It must be possible to direct any measures against the 'controlling mind' because entities which are engaged in tax avoidance and tax evasion will often be fronted by a third party with little active involvement and no asset backing. Again, this would be more easily achievable using the transfer of liability approach.
20. We understand from our meeting with HMRC officials that they have concerns around transfer of liability where more than one individual is involved – and would want to ensure that they could maximise the tax recovery. We therefore suggest that providing for Transfer of Liability on a Joint and Several basis should be considered. This would make each person served with a Transfer of Liability Notice jointly and severally liable for the tax shortfall following insolvency.
21. Appropriate safeguards are extremely important to ensure that there is public confidence in any new measures - and to ensure that only those who are intended to be caught are brought within scope.
22. In addition to safeguards such as a right of appeal to a tax tribunal, we believe that using the STAR criteria and 'deliberate' behaviour (see paragraphs 13 to 16 above) as the conditions for being within the scope of the new measures, would provide a significant safeguard against individuals being caught unintentionally.
23. The Insolvency Act 1986 provides for a number of remedies against directors and officers of a company where their behaviour or actions fall short of the expected standards. We anticipate that where the proposed measures are triggered it is likely that an insolvency office holder will also be pursuing, or contemplating pursuing, action against a director. Given that in some cases there will be restricted prospects of recovery from a director, due to the available assets, conceptually at least this would result in a race between HMRC and the insolvency office holder to obtain a recovery first.
24. The office holder is acting for all creditors, and in the event of a recovery from a director this would be distributed in accordance with rules set out in insolvency legislation. A recovery by HMRC, outside the insolvency process, would result only in a recovery for HMRC which could potentially be to the detriment of other creditors. Safeguards should be put in place to prevent an unintended 'super preference' being obtained by HMRC through the introduction of the proposed new measures. For instance, it may be appropriate that a Transfer of Liability Notice should only be issued after the insolvency office holder has confirmed that they do not intend to pursue an action under the Insolvency Act 1986, or that any action under the Insolvency Act 1986 has been completed.

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