



Briefing on Tax and Insolvency

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What I hope to cover

1. Kicking the can down the road into a perfect storm.
2. The reintroduction of Crown Preference.
3. The SME CVA.
4. Members' voluntary liquidations and the assignment of directors' loans in satisfaction of shareholder distributions.
5. Overdrawn Directors' Loan Accounts in liquidation; the charge to income tax.
6. Miscellaneous: Payment of CGT on the sale of property in bankruptcy within 30 days.

1. Kicking the can down the road into a perfect storm (1).

- Deferral of tax payments
 - VAT: UK VAT registered businesses with a VAT payment due between 20 March 2020 and 30 June 2020, had the option to defer the payment until 31 March 2021 (now payable in smaller payments up to the end of March 2022, interest free). HMRC estimates circa £28bn deferred to March 2021 (although some now payable by instalments).
 - Income tax for individuals: 31st July payment on account payable by 31st January 2021 BUT will also need to pay top up payment and first payment on account. N.b. possible reduced payment on account if profits affected by covid-19 but depends upon when the accounting period ends (may end before the profits were affected). Possibility to apply online for TTP if tax below £30,000; otherwise, looked at on a case by case basis.
 - Corporation Tax and PAYE: no specific scheme but on a case by case basis. HMRC have generally been sympathetic to 3 month deferral. N.b. companies pay tax 9 months and 1 day after the end of the accounting period so 1st January 2021 for accounting periods ending 31st March 2020.
 - Quarterly Instalment Payments (“QIPs”): if already paid may make a claim for repayment under Regulation 6 of SI 1998/3175.
- Brexit
 - Possibility of leaving with an “Australian trade agreement” (i.e. no trade agreement) on 31st December 2020.

1. Kicking the can down the road into a perfect storm (2).

What are Australia-style arrangements?

Downing Street started using the term at the beginning of the year as a more palatable shorthand for a no-deal. The EU does not have a free-trade deal with Australia, although they are in negotiations. The two sides operate mainly on World Trade Organization (WTO) rules, with huge tariffs on imports and exports.

It would be more accurate to describe the outcome that would be secured by a no-deal as an Afghanistan-style arrangement, given the lack of formal cooperation in that trading relationship. This is because the EU does have a few agreements in place with Australia that it would not have with the UK in the event of a failure of the trade and security negotiations. These include an agreement on the transfer of EU passenger name records to Australian border authorities to help combat crime and terrorism and an agreement on the mutual recognition of conformity assessments, so that a product tested to EU standards in Australia is regarded as compliant, eliminating the need for duplicative testing when it is imported.

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1. Kicking the can down the road into a perfect storm. (3).

- Individual
 - VAT: 31st March 2021 deferred payment and usual VAT in the quarter depending when it is (possibility of some deferral).
 - Income tax: 31st January 2021 Payment on account for July 2020; top up payment for accounts ending before 6th April 2021 (probably at pre-covid-19 levels) and 1st payment on account (possibly reduced for lower profits during covid-19 period).
 - PAYE: if TTP probably needs paying soon.
 - Brexit: possible higher prices due to import tariffs, pressure on margins or higher prices passed on to consumers, lower turnover due to higher prices and reticence to spend due to customers threat of redundancy (will we spend before Christmas if threat of redundancy and covid-19 restrictions still in place?).
 - JRS: did they get it right? Possibility of enquiry.

1. Kicking the can down the road into a perfect storm. (4).

- Company
 - VAT: 31st March 2020 deferred payment and usual VAT in the quarter depending when it is (possibility of some deferral).
 - Corporation tax: 1st January 2021 possibility of CT tax payments for y/e 31st March 2020 (a popular date).
 - PAYE: if TTP then probably needs paying soon.
 - Brexit: possible higher prices due to import tariffs, pressure on margins or higher prices passed on to consumers, lower turnover due to higher prices and reticence to spend due to customers threat of redundancy (will we spend before Christmas if threat of redundancy and covid-19 restrictions still in place?).
 - JRS: did they get it right?

2. The reintroduction of Crown Preference (1).

- *Enterprise Act 2002*: Abolition of Crown Preference.
 - Introduction of the prescribed part £600,000.
- *Finance Act 2020*: Introduction of Crown Preference with effect from 1st December 2020.
 - Increase in prescribed part to £800,000 for floating charges given after 6th April 2020.
- Amendment to s386, IA 1986 and insertion into Schd 6 to IA 1986 of a new paragraph 15D and amendment of s286(1B) to add paragraph 15D to class of secondary preferential debts. (*Category 9: Certain HMRC debts.*)
 - Applies to Bankruptcy and IVAs, Administration, Liquidation and CVAs.
- If the relevant date (s387, IA 1986) is on or after 1st December 2020 the debts are preferential. This includes bankruptcies, IVAs and CVAs. Therefore, the amount needs to be quantified and agreed with HMRC.

2. The reintroduction of Crown Preference (2).

- Which taxes does it apply to?
 - VAT;
 - PAYE (inc Student loan repayments);
 - Employees NICs; and
 - Construction Industry Scheme deductions.

"This clause achieves this by amending insolvency legislation to make HMRC a secondary preferential creditor [for] certain debts due to HMRC. The debts included are VAT and through the making of regulations by HMRC, other taxes or amounts due to HMRC paid by employees or customers through a deduction by the business for example from wages or prices charged such as PAYE (including student loan repayments), Employee NICs and Construction Industry Scheme deductions.

HMRC will remain an unsecured creditor for taxes levied directly on businesses, such as Corporation Tax and Employer NICs."

- After 1st December 2020 this will include amounts of VAT and PAYE which have been deferred because of Covid-19 (inc £28bn of VAT).
- N.b. although the legislation provides for regulations to limit the time period HMRC can go back none have been made. The period is currently unlimited.

2. The reintroduction of Crown Preference (3).

- Further Issues:
 - VAT groupings, can you break the group to prevent joint and several liability?
 - Employees in a separate company?
 - Lenders already factoring in and immediately providing therefore less to lend.
 - Cliff edge on 1st December 2020?
 - New notifications to lenders if borrower to make late payment of tax debt.
 - Consensual restructuring instead of enforcement?
 - HMRC tax clearance? How long? Several months not unusual. Effect on distributions.

3. The SME CVA

- R3 Standard Form Covid-19 CVA Proposal and Standard Conditions
 - R3 STANDARD FORM COVID 19 CVA PROPOSAL. Version 1. September 2020. England and Wales
 - <https://www.r3.org.uk/stream.asp?stream=true&eid=22956&node=314&checksum=D784AE59439775C438EF2599613703DE>
 - Standard Conditions for Company Voluntary Arrangements. Version 1
 - <https://www.r3.org.uk/stream.asp?stream=true&eid=22951&node=314&checksum=F8A7C12C854ED7923124FBD7D5893FDD>
 - Comparison IVA Standard Terms. Standard Conditions for Company Voluntary Arrangements. Version 1.
 - <https://www.r3.org.uk/stream.asp?stream=true&eid=22952&node=314&checksum=34AFDB6D18BE3E84EA06151C839F81EB>
 - EXPLANATORY NOTE FOR INSOLVENCY PRACTITIONERS
 - <https://www.r3.org.uk/stream.asp?stream=true&eid=22953&node=314&checksum=66E824030CBA366195D53EAC8FBF5C57>

3. The SME CVA

- R3 Standard Form Covid-19 CVA Proposal and Standard Conditions
 - Paragraph 70: Overdue accounts and returns 2 months
 - Paragraph 73: Tax liabilities arising on realisations
 - Liabilities to be proved: HMRC say those to the last accounting date. So those in the period between the last accounting date will be payable as normal in the CVA. May bee beneficial to delay over an accounting date if, for example, 11 months have elapsed since the accounting date. Consider shortening the accounting period? HMRC's attitude?
- Explanatory note.
 - Paragraph 4: Position of HMRC.
 - HMRC Guidance 26 June 2020.



Voluntary Arrangements – HMRC's position going forward

This note explains HMRC's approach to variations and new proposals in respect of Individual Voluntary Arrangements (IVAs), Partnership Voluntary Arrangements (PVAs) and Company Voluntary Arrangements (CVAs) from 1 July 2020 until 30 November 2020.

Existing arrangements

Some companies or individual debtors with voluntary arrangements believe they'll continue to have difficulty in paying contributions because of COVID-19. In these cases, supervisors can use any discretion within the terms of the arrangement to allow a contribution break without reference to creditors.

For IVAs where the IVA Protocol Standard Terms and Conditions apply, clause 8(8) allows flexibility. For arrangements where this isn't an option, the supervisor should work with the debtor or company to understand whether the arrangement as it stands remains viable, or whether it would be viable if varied. This is a matter for case-by-case consideration and HMRC will not support 'mass variations' in connection with COVID-19.

For companies and individuals where the HMRC liability arises from on-going trading, our support is given provided payment of post voluntary arrangement (VA) taxes is a priority.

We recognise that paying these taxes whilst maintaining VA contributions will be a challenge for some as we emerge from the pandemic. We will support variation of proposals:

- to allow contribution breaks in each of the two years following approval of the variation; these can be taken in aggregate or as on cases where the supervisor is satisfied that they are necessary and that they will enable post-VA taxes to be paid on time and in full
- to allow any fixed duration to be extended to allow a catch-up of missed contributions.

We may also:

- support a longer contribution break in appropriate cases, where this is likely to ensure the longer-term viability of the arrangement
- agree to the deferral of equity realisation where the current situation prevents the debtor or company from complying with the existing deadline.

We will look critically at variations that seek to end the arrangement early. We are unlikely to support the removal of asset realisation clauses in any but the most exceptional circumstances.

New proposals

HMRC will continue to look at proposals within the framework set out in the [VAS help-sheet](#).

The impact of COVID-19 means that a good history of paying taxes on time may no longer be a reliable indicator for individuals or companies proposing a voluntary arrangement. We are reliant on practitioners to report as fully as possible on the nature of the business, the impact of COVID-19 on its trade, what countermeasures have been taken and to bring their professional judgment to bear on the viability of the business and voluntary arrangement.

For those with a longer, less positive history, this objective reporting is even more critical. It should explain pre-COVID-19 tax arrears, as well as the impact of the pandemic on that business.

On new proposals, we again see payment of post-arrangement taxes as vital. We would ask that practitioners look critically at how this can be achieved. Depending on the circumstances of the debtor or company, we would support a flexible approach, looking positively at:

- variable contributions from the outset to accurately reflect cash-flow variations, and some limited flexibility for supervisors to reduce contributions temporarily
- contribution breaks in years one and two, as outlined above, to enable the debtor or company to pay taxes as they fall due.

Given the substantial support that has been provided, we would also expect to see that PAYE and National Insurance Contributions (NICs) arising from Coronavirus Job Retention Scheme (CJRS) payments have been paid. If not, these must be treated as priority payments in the arrangement, ahead of all other unsecured creditor claims (including other elements of HMRC's claim).

A condition of the CJRS grant is that related PAYE tax, employer NICs and pension contributions due on wages are paid. Until 31 July, a claim can be made for these for the hours the employee is on furlough. From 1 August employers will no longer be able to claim for employer NICs and pension contributions.

If you think the taxpayer may struggle to pay outstanding tax liabilities, please contact us as soon as possible. They may be eligible to receive support with their tax affairs through HMRC's Time to Pay service.

4. Members' voluntary liquidations and the assignment of directors' loans in satisfaction of shareholder distributions.

- Loans to Participants - general.
 - If the company is a CLOSE COMPANY and the director is a PARTICIPATOR or an ASSOCIATE of a participant:
 - A loan to the director will result in the company being liable to pay an amount of corporation tax equal to the dividend upper rate for the tax year on which the loan or advance is made (s455, CTA 2010).
 - Payable on the day following the end of the period 9 months from the end of the accounting period in which the loan or advance is made.
 - Anti-avoidance provisions to prevent loans being repaid and subsequently re-advanced.
 - If the loan is subsequently repaid or released, the s455 tax is repaid to the company (s458, CTA 2010) but it is repaid on the day following the end of the period 9 months from the end of the accounting period in which the loan or advance is repaid.
 - If the loan is released or written off the director is liable to INCOME TAX on the amount of the debt released or written off in the tax year and the amount is treated as income. s415, ITTOIA 2005

4. Members' voluntary liquidations and the assignment of directors' loans in satisfaction of shareholder distributions.

- The basic position in liquidation (CTM61558).
 - Where repayment is made or the loan is written off:
 - Any s455, CTA 2010 (or s464A) tax will be repaid to the company (date for repayment?)
 - The shareholders are entitled to a proportionate share of the assets available in the winding up; this will include the receivable represented by the overdrawn director's loan account.
 - The legislation is quite clear. The distribution of assets in a winding up is not a distribution within the meaning of Part 23 , CTA 2010 (section 1030, CTA 2010). It is a transfer of assets and liabilities between the company and its members and is a capital distribution for the purposes of s122, TCGA 1992. Thus where there are net assets to be distributed, the shareholders are entitled to treat the value distributed to them as a capital gain and to claim business asset disposal relief (formerly entrepreneurs' relief) as appropriate.
 - Subject ultimately, to s396B, ITTOIA 2005.

4. Members' voluntary liquidations and the assignment of directors' loans in satisfaction of shareholder distributions.

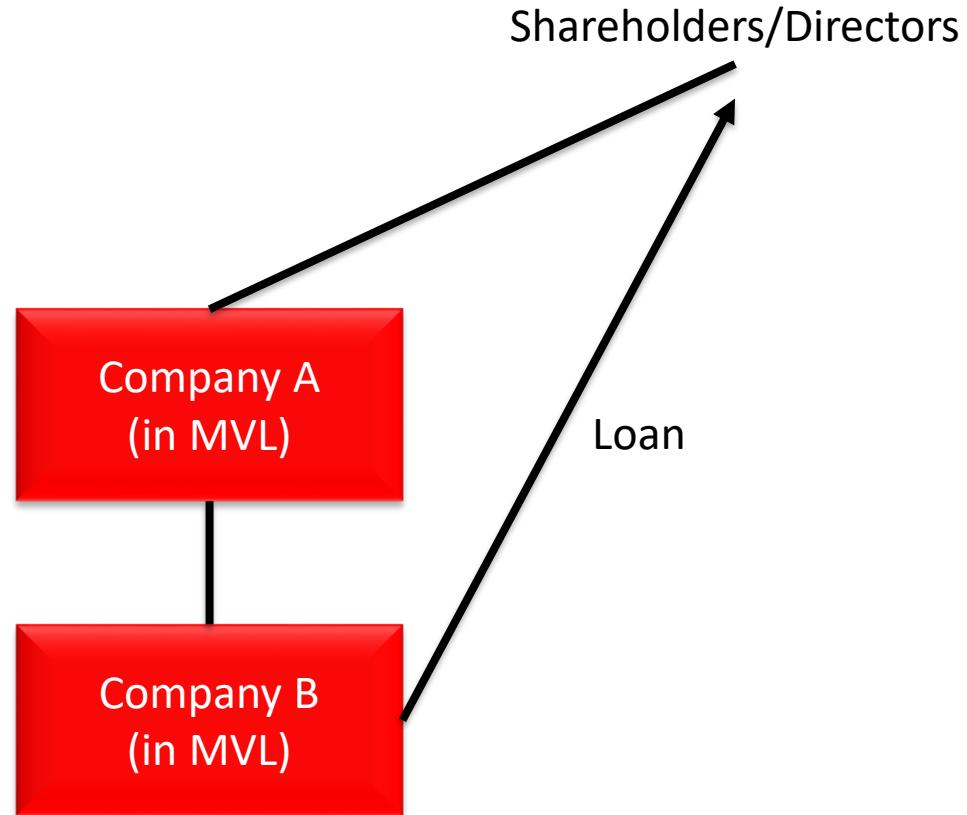
- The position in MVL (CTM61559).
 - HMRC note that these are solvent liquidations. The shareholders (participants) are entitled to receive the value of the net assets from the company. At the same time the shareholders owe the company the amount of their overdrawn loan accounts.
 - Shareholders could repay and then would be entitled to receive the full amount of the value of the net assets as a capital distribution.
 - Otherwise, they can set-off the value of the assets due to them against their debt and only withdraw the net amount.
 - Where two debts are set-off in this way this way, this will constitute a repayment.
 - There is no question of s415, ITTOIA 2005 applying.

4. Members' voluntary liquidations and the assignment of directors' loans in satisfaction of shareholder distributions.

- The position in MVL (CTM61559).
 - Example
 - A participator owed the company £1,425,000 by 30 May 2017. The company went into Members' Voluntary Liquidation on 1 June 2017. The net assets, including the overdrawn loan account totalled £5,300,000.
 - On 1 June 2017 the liquidators declared an interim distribution in the liquidation of £1,425,000 per £1 ordinary share, giving a total distribution at that date of £1,425,000. This was not paid out in cash to the shareholder but was credited to his loan account. It would be a capital distribution within s122, TCGA 1992. This is not a release of the loan, it is a repayment of the loan. There can be no charge under s415, ITTOIA 2005.
 - Likewise any further distributions in the liquidation up to the total balance of the net assets will also be capital distributions.

4. Members' voluntary liquidations and the assignment of directors' loans in satisfaction of shareholder distributions.

- Issues.



5. Overdrawn Directors' Loan Accounts in liquidation; the charge to income tax.

- The position in Insolvent Liquidations and Dissolutions. (CTM61560).
 - HMRC notes:
 - The liquidator should seek repayment of any loans or, if repayment is not made, should release or write off any outstanding loans.
 - Where the whole or part of a loan is written off s458, CTA 2010 relief will be due and any s455, CTA 2010 tax repaid.
 - Where the whole or part of a loan is written off there would be a charge under s415, ITTOIA 2005 on the person to whom the loan was made and Class 1 NIC will be chargeable if the participator or associate was an employee if it is remuneration or profit derived from an employment (s3(1) SSCBA 1992). This was confirmed in the First Tier Tribunal in *Stewart Fraser Ltd v HMRC* [2011] UKFTT 46 (TC).

5. Overdrawn Directors' Loan Accounts in liquidation; the charge to income tax.

- The position in Insolvent Liquidations and Dissolutions. (CTM61560).
 - Example 1
 - Director loan account £1m overdrawn at date of liquidation.
 - Balance of company assets (i.e. net of creditors but including the DLA), £500k
 - The shareholder will be due a distribution, chargeable to capital gains tax in the amount of £500k (the net assets). The distribution will repay £500k of the overdrawn loan account (by set off), and relief under s458, CTA 2010 will be due to the company on that amount. However that still leaves the shareholder owing £500k.
 - Where the liquidator releases or writes off the balance, it would be chargeable on the shareholder under s415, ITTOIA 2005. Where the liquidator and participator enter into a settlement agreement where the partial payment is expressed to discharge the participator's obligations in full, or in "full and final settlement" of amounts owing to the company, this also amounts to the release or write-off of the balance.

5. Overdrawn Directors' Loan Accounts in liquidation; the charge to income tax.

- The position in Insolvent Liquidations and Dissolutions. (CTM61560).
 - Example 2
 - Director's loan account £1m overdrawn at the date of the liquidation.
 - Balance of company assets (i.e. net of creditors), including DLA, a negative balance of £200k.
 - Here there is no distribution of assets available to the shareholder, he therefore still owes £1m to the company. Again if this is released or written off then the shareholder will be charged on that amount under s415, ITTOIA 2005.
 - A charge under s415, ITTOIA 2005 is the right result where there is a loan outstanding after any capital distributions have been made as clearly the shareholder has had the funds out of the company, untaxed, prior to the liquidation.

5. Overdrawn Directors' Loan Accounts in liquidation; the charge to income tax.

- The position in Insolvent Liquidations and Dissolutions. Loan irrecoverable. (CTM61561).
 - Loan irrecoverable.
 - It may be that tax has not been paid under s455, CTA 2020.
 - HMRC will be a creditor (unsecured) for that amount.
 - Has been argued that should be waived because will prejudice other creditors.

5. Overdrawn Directors' Loan Accounts in liquidation; the charge to income tax.

- Aggregating accounts. (CTM61565).
 - Separate accounts or a single joint account?
 - Question of fact.
 - Section 455, CTA 2010 follows the actual arrangements between the parties as evidenced by the company's accounting books and records and the general law on debts and repayments.
 - Accounts may be kept separate.
 - Section 455, CTA 2010 consequences follow where one account is overdrawn even if another account is in credit.
 - Netting will be allowed from the date of book entries.

5. Overdrawn Directors' Loan Accounts in liquidation; the charge to income tax.

- *Collins v Addies (HM Inspector of Taxes) [1992] BTC 532.*
 - Sale of shares and novation of debt amounted to a release.
- Novation
 - If the debt is novated it has been released and not repaid. Section 458, CTA 2010 relief would be due on the original debt, and s415, ITTOIA 2005 may apply. Depending on the facts, the new loan may also be subject to a new charge under s455, CTA 2010.
- Assignment
 - Relief under s458, CTA 2010 may or may not be due in the case of an assignment; this will depend on the facts. Has the loan from the close company actually been repaid or is it still outstanding, albeit from a different debtor? How exactly is it that the original debtor no longer owes the money?

6. Miscellaneous: Payment of CGT on the sale of property in bankruptcy within 30 days.

- Recent changes to the payment dates for CGT mean that where a property is sold the CGT is due 30 days after the sale.
- Trustees in bankruptcy theoretically liable to pay but may not have details of the debtor's circumstances.



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