Resolving the conflict

Management of taxes | OMB | Personal tax



01 July 2019

Michael Avient provides insight on the conflict between the right to possessions and the 2019 loan charge

Key Points

What is the issue?

Does the 2019 Loan Charge interfere with the peaceful enjoyment of possessions contrary to Article 1 Protocol 1 (A1P1) to the ECHR?

What does it mean to me?

Many of those liable to the 2019 Loan Charge have yet to settle, and in the absence of a successful judicial review challenge, those who do not settle will be liable to the

charge.

What can I take away?

Retrospectivity in itself is not sufficient to engage A1P1, it will also be necessary to evidence the existence of a possession, the law was arbitrary, and it was not proportionate. Evidence obtained by the All-Party Parliamentary Loan Charge Group may give significant grounds for such a challenge.

In 2005, the current Chancellor of the Exchequer said: ‘A taxpayer is entitled to know with certainty… what he may or may not do in planning his affairs… [and] is entitled to be protected from retrospective and retroactive legislation’.

It is difficult to square the 2019 Loan Charge, introduced by Finance (No 2) Act 2017, Sch 13, with this statement.

The self-assessment system is built on strict time limits, which apply to taxpayers and HMRC alike. Enquiries must be opened within 12 months and in the absence of an enquiry, the self-assessment becomes final and the tax year closed. The tax year may only be reopened if HMRC issue a discovery assessment within specified time-limits.

At a stroke, the 2019 Loan Charge removes all these time-limits, providing that all employment related loans entered after 5 April 1999, which remain ‘outstanding’ on 5 April 2019, are chargeable to tax as employment income in 2018 /19.

It is on this ground that the legislation may be characterised as retrospective or retroactive.

The principles

By nature, tax interferes with an individual’s right to possessions, however it is warranted due to the benefits afforded to the overall community. The underlying aim of the law is to regulate this relationship between the State and the Individual. In measuring the ‘quality’ of that relationship, terms such as ‘justice’ and ‘fairness’ are used as embodied in the concept of the ‘rule of law’.

Any legislation seeking to change the legal outcome of an action, after it has occurred and cannot be modified or changed has the real danger of damaging the

quality of that relationship. However, retrospective legislation may be found to be valid where those affected have been warned or have some knowledge of what to expect and can therefore decide how to act.

The power of Parliament

The definition of retrospective legislation which has received judicial approval, is a statute: '…which takes away or impairs any vested right acquired under existing laws, or creates a new obligation, or imposes a new duty, or attaches a new disability in respect to transactions or considerations already past'.

In the UK there are no 'constitutional fundamentals'. The only restriction on the power of Parliament to pass retrospective legislation lies in the ECHR, as incorporated into UK law. As Lord Neuberger said in his 2011 lecture 'Who are the masters now?': 'Parliament's legal omnipotence means that Parliament can retrospectively render lawful an action which was contrary to the law at the time it was done'.

European Convention on Human Rights

Taxation has been generally excluded from the scope of human rights law. In *Ferrazzini v Italy* it was held that tax law belonged to public law rather than private law, so that: 'tax matters still form part of the hard core of public authority prerogatives, with the public nature of the relationship between the taxpayer and the tax authority remaining predominant.'

In APN cases such as *Rowe* and *Walapu* this principle was regarded as of itself giving rise to the blanket exclusion of human rights considerations from tax matters.

However, A1P1 provides for the individual's peaceful enjoyment of possessions and they should not be deprived of them except in the public interest. Notwithstanding the wide margin of appreciation given to the State, there must be a fair balance between the public interest and the interests of the individual.

A, B, C & D v UK considered A1P1 and held in that case that retrospective tax legislation was proportionate. However, what appeared to weigh heavily on the Commission's mind was the effectiveness of the tax avoidance was already in doubt combined with its secrecy, uncommercial nature and artificiality.

In *Provincial Building Society v UK*, again, a fair balance was found to exist. The legislation was required to give effect to the original intention of Parliament and prevent a windfall to taxpayers simply because of inadvertent defects in the legislation.

The 2019 Loan Charge

Any judicial review of the 2019 Loan Charge faces very significant hurdles. The charge is contained within primary legislation, and its retrospectivity must have been intended by Parliament.

HMRC publications have consistently asserted the legislation is not retrospective and emphasised its fairness and proportionality. However, this view appears problematic because:

- HMRC have always emphasised the loans were not going to be repaid, however if this was the case, the loans could not in law be loans;
- If repayment is envisaged, the loans cannot be an asset but a liability;
- Published settlement terms are based on the amount contributed to the arrangements and not the loans; and
- HMRC require settlement of closed years.

As far as the author is aware two judicial reviews have been lodged, both seeking to challenge the legislation under A1P1. The first has already received permission to proceed.

Possession

In *R (Robert Huitson) v HMRC* the nature of possession was considered, and in that instance, it was found that there only existed a ‘disputed claim’ which could not amount to a possession. In *R (APVCO and others) v HMRC* the taxpayer actually held the cash, but it was held to be impressed with an arguable claim by HMRC. All the retrospective legislation did was put the disputed question as to the payment of tax beyond doubt.

In contrast, the 2019 Loan Charge bites where the tax year is closed or where a settlement agreement already exists. In these instances, there can be no question of the cash being impressed with a claim by HMRC.

Open enquiries often relate to employer payments to third parties, as opposed to the loan to the taxpayer. In such instances, it is difficult to see how the receipt of a loan (which must be at least technically repayable) can be impressed by any claim by HMRC. Absent of such an impressed claim, the cash held will be a possession.

Proportionality

Even where a possession exists, it is necessary to show the legislation is not lawful and proportionate. *NKM v Hungary* found retrospective legislation warranted to correct 'technical deficiencies' in law where justified in the public interest. The fact that only general warnings had been issued by the State regarding acting against specific schemes did not make the law arbitrary.

Ensuring the charge bites in the absence of enquiries, and the failure to target the legislation in relation to payments to third parties, may lead to a conclusion of arbitrariness. Although targeted at specific schemes, its generality must bring into question whether its wording is sufficiently precise to be foreseeable in effect. Certainly, it appears that HMRC are still struggling to identify all types of arrangements which may be caught.

The wide margin of appreciation given to the State and recognised in cases such as Rowe means any challenge will face very real difficulties. However, the wide-ranging evidence obtained by the Loan Charge All-Party Parliamentary Group may shift the scales. Most notable are findings in their report that:

- There is a clear risk to the mental welfare of people facing the charge;
- Many bankruptcies will result from the charge;
- The original impact assessment published by the Treasury was flawed and inadequate, to the point of being negligent;
- The real reason for the introduction of the charge was to bypass normal legal processes and allow HMRC to collect tax 'out of time' under existing legislation; and
- A cynical campaign of misinformation was waged by HMRC and the Treasury.

If these findings are upheld in any subsequent review, it is difficult to see how any court could find the legislation proportionate as currently enacted. What is certain, is that the evidence gathered has provided those judicially reviewing the legislation with far greater data regarding its enactment and implementation than has

previously been available to those making challenges under A1P1.

Conclusion

Those seeking to challenge the 2019 Loan Charge legislation under A1P1 face significant challenges. However, the breadth of the legislation, its imposition on loans dating back 20 years, the effects it is having on those taxpayers affected and the growing criticism by MPs and some professional bodies may mean that there is now the impetus for the courts to decide the wide boundaries of the margin of appreciation of the State in tax matters have finally been breached.

Editor's Note: Finance Act 2019 required the publication of a review into the loan charge. Details of this and other matters can be found in a House of Commons library briefing. HMRC has issued various comments on the loan charge: HMRC issue briefing: charge on disguised remuneration loans and Tax avoidance loan schemes and the loan charge.