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CLIENTS PAYING EMPLOYEES IN CRYPTOCURRENCY?

Are your clients increasingly starting to ask about paying employees in cryptocurrency and are you qualified to advise them?

Cryptocurrency, cryptocoins, cryptoassets, Bitcoin, Cardano, payment tokens, Ethereum, exchange tokens, – all words which are becoming increasingly common in everyday language, can be roughly translated as "virtual money's worth".

Increased appetite for cryptocurrency

Virtual money's worth appears to carry all the hallmarks of a high-risk investment – but that is not stopping people from investing in it. According to the Payment Services Regulator (PSR), the market is now worth £1.6 trillion globally and over 2.3 million people now own a cryptoasset in the UK – the average investment holding being around £300.

With suggestions now doing the rounds that it may be possible to purchase cars with Bitcoin, for example, or that virtual money could eventually become legal tender, it's easy to see how some directors and employees may develop an appetite for being paid in cryptocurrency or in benefits-in-kind (possibly using a form of virtual salary sacrifice) which have been purchased by these means.

Where do you and your clients start to navigate the maze, and how does UK payroll and taxation fit into the equation? It is important to note that employees working overseas may be treated more, or less, favourably as far as being paid by cryptocurrency is concerned.

For example, in China cryptocurrency is illegal and it is not possible to exchange it for traditional currency, whereas in Europe and the US, this is not the case.

Keeping up with the pace of change

It is probably worth reading up on exactly what 'blockchain' (the technology behind cryptocurrencies) is – ICAS has numerous resources to read up on - and what the PSR has to say about it all. They have recently referenced a 2019 white paper by Diem's in the US which speaks of the use of a crypto-wallet which could be utilised to make payments using PayPal, for example.

The Financial Conduct Authority (FCA) has also conducted research that points towards the use of virtual money in transaction rapidly becoming the norm.

However, norms are often accompanied by complacency. How much trust can be placed in a currency that is not currently traceable or regulated and, with that in mind, should it be used as a means to pay and reward people?

Risky business?

The UK Government is currently working with other jurisdictions and the global banking sector considering

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how to regulate cryptoassets. It is important to note that the FCA does not regulate most cryptoassets and they emphasise that investments in unregulated cryptoassets are therefore unprotected. Agents and employment tax advisors generally should consider the risks for themselves and clients in this complex and relatively opaque area.

The FCA has set up a cryptoasset page to raise awareness of this and provide information to the public. They recommend that independent financial advice should be sought from a suitably qualified professional when considering such investments. Their top four considerations are:

1. Volatile value

The market value of cryptoassets can be extremely volatile. You could lose a lot, and quickly. It is also worth remembering that there are many competing blockchain companies looking for your investment and that some will inevitably fail.

2. Theft

Cryptocurrencies can only be bought and sold on cryptocurrency exchanges. These exchanges are a tempting target for hackers and security breaches have led to the theft of digital currency, with not all investors getting their money back.

3. Hard to spend

You cannot spend cryptoassets like cash as few retailers accept cryptocurrency such as Bitcoin as payment. So, generally you must sell them on an exchange, with their associated security issues. If you are storing your cryptoassets on a password-protected personal hard drive or memory stick and you lose or forget the password, you may well have lost access to your investment altogether.

4. Unregulated

Cryptoassets are largely unregulated. If your investment is stolen, there is not a straightforward way to get your money back, and FSCS cannot protect you. As the industry is still developing, there are frauds involving cryptoasset investments that are hard to distinguish from genuine investment opportunities.

Cryptocurrency and employment tax implications

When faced with having to answer client questions on cryptocurrency in the context of employment related remuneration planning, it is easier to break this concept down and see it for what it really is – employment earnings.

If someone is a statutory director or employed under a UK employment contract and they are a UK taxpayer then the method of payment is largely irrelevant because an income tax (PAYE) liability applies to it, whether it is 'money' or 'money's worth'. Cryptocurrency is capable of being converted into traditional money and therefore it is defined as 'money's worth' by HMRC.

Back to reality, then, courtesy of s.62 ITEPA 2003. The Benefits Code within ITEPA 2003 will also apply to any benefits in kind provided by way of cryptocurrency. HMRC's Cryptoassets manual replaced the two original manuals, 'Cryptoassets: tax for individuals' and 'Cryptoassets: tax for business' on 30 March 2021. The new manual was last updated on 22 February 2022.

HMRC internal manuals at CRYPTO42050 discusses making payments to employees and where pension contributions are made with cryptocurrency, this guidance can be found at CRYPTO43000.

NICs

The NICs legislation at s.3 SSCBA 1992 mirrors the tax legislation – so what is deemed to be employment earnings for tax purposes is also employed earner's earnings for NICs purposes. HMRC internal manuals at CRYPTO42200 discusses the National Insurance treatment. Benefits in kind provided by way of cryptocurrency should be declared on P11D and attract Class 1A NICs, just like any other benefit in kind.

A note on National Minimum Wage

At present, ICAS is waiting for confirmation from BEIS policy teams on whether cryptocurrency is classified as 'pay' for NMW purposes. It is considered unlikely, due to the fact that cryptocurrency is not a regulated currency. It is therefore probably prudent, in the absence of advice to the contrary, to ensure that an employee or worker who is eligible to receive NMW is paid at least that part of their salary in cash or 'fiat money' (inconvertible paper money made legal tender by a government decree) to ensure that an NMW breach cannot be deemed to have occurred.

Further guidance is also provided in the HMRC manuals on the tax treatment of benefits provided by third parties and payments which are not readily convertible assets.

Many tax experts who are now regularly involved in the cryptoasset advisory space are in disagreement with HMRC about their classification of Cryptoassets as "money's worth" – however, until regulation followed by legislative provisions and tax cases collectively come into play down the line, the Cryptoasset Manual is what we have to work with, and HMRC's position is clear.

CONTRACTING OUT AUDIT WORK

ICAS is conscious that there is currently great demand for audit staff but that it can be extremely difficult to recruit. What can a firm do to mitigate staff shortages in audit? One possibility is to contract out some of the audit work, but if so, what considerations should inform the decision.

Typically, when we see the use of subcontractors, it is as an isolated situation, with one individual acting for a firm, for example conducting one specific part of the audit such as a stock take. Wider contracting out may lead to significant additional review risks if whole pieces of audit work are to be outsourced, for the firm to control work, and for external oversight (for instance by ICAS when scheduling monitoring visits).

In terms of the Audit Regulations, a sub-contractor or a consultant who conducts audit work for an audit firm is considered like any other “employee”. Specific reference is made to such an arrangement in the following regulations:

- AR 3.06 - the regulations specifically require ‘fit and proper’ checks to be done. AR3.06 also states that “*When a registered auditor sub-contracts work to another firm or an individual, whether registered or not, there should be a formal engagement letter or contract. This should make clear who is responsible for the various parts of the accountancy and audit work. A sub-contractor should be treated as an employee for the purposes of the work. Where this involves firms or personnel in another country, fit and proper assessment needs to be exercised and adapted within the confines of the law of that other country and appropriately documented”*
- AR 3.12 – “*all the audit working papers created by the other firm have to be returned to the registered auditor for retention in accordance with regulation 3.11. Alternatively, the other firm may keep the papers. In this case the registered auditor must make sure that the other firm will keep the papers for as long as the auditor would. Also, the registered auditor must have the right to have access to those papers at any time and retrieve them if necessary. As with papers held directly by the registered auditor, any decision to destroy the papers should be made by the registered auditor and not the other firm…Whatever arrangements are made between two firms, they should be recorded in a suitable letter of engagement or contract.”*

In practice, ICAS monitoring would be looking for these forms/documents above during a visit, but also want to understand how the firm had adequately assured itself of competence, integrity, and the overall quality of the audit work – and the amount of monitoring work around this would reflect the extent of the outsourcing and, no doubt, be well over and above the approach taken over a standard employee.

Beyond the audit regulations, there are also other regulatory areas that would need considered. In particular:

- AML - The use of a sub-contractor would require the firm to update their policies and procedures to reflect the relationship and ensure that the sub-contractor is part of their AML reporting regime. In addition, they would need to consider the AML training requirements for the sub-contractor and consider how they will satisfy themselves about the sub-contractor’s compliance with the firm’s policies and procedures.
- UK GDPR – careful consideration will be needed of GDPR compliance. The firm would probably have to proceed based on the assumption that personal data will be involved in the audit somewhere along the line (either that of employees, or of an individual as a customer or a supplier, etc.) and therefore the usual issues of processing data would apply. There may also need to be consideration of whether the contractor is a data processor or data controller and, if outsourced beyond the UK, there may be possible issues around data being held or processed out with the UK, appropriate contractual obligations provided for, etc.
- PII – the firm would need to notify its PII insurer and ensure that the sub-contractor’s work is covered.
- Cyber security – what arrangements are to be put in place re access to systems and/or secure exchange of data.
- Code of ethics – how will compliance with the ICAS Code of ethics be monitored.

Outsourcing may provide a solution to temporary staffing issues but if so, the firm’s regulatory and quality control aspects should be carefully reviewed before doing so.

SHOULD IT TAKE FOUR HEARINGS TO DECIDE EMPLOYMENT STATUS?

Another two IR35 cases were decided recently, which furthered the cause of HMRC in their pursuit of television and radio presenters when the Court of Appeal found in favour of HMRC in both instances.

Kickabout

The first decision, known as the Kickabout case, concerns Paul Hawksbee, a Talksport radio presenter. The First Tier Tribunal found for Mr Hawksbee's company and the Upper Tribunal then reversed the decision, finding for HMRC. ICAS reported on this case in 2020 and that article explains the decision up to that point in more detail.

The Court of Appeal upheld the upper Tribunal's decision, in which it had been concluded that mutuality of obligation was present and the level of control over Mr Hawksbee by the radio station in terms of production and direction pointed to a hypothetical contract of employment.

Mr Hawksbee had argued that he was placed at increased levels of financial risk due to the relative instability of the contractual terms. The contract was a rolling fixed-term two-year contract which placed an obligation to be renegotiated genuinely and without malice for extensions to that contract.

Bearing in mind Mr Hawksbee had worked for Talksport radio for 18 years, albeit only a handful of tax years were being examined during the case proceedings, the judge found his claims of financial risk and instability hard to swallow and found for HMRC.

Atholl House

The second case is related to Atholl House, a company owned by the Loose Women presenter Kaye Adams. In this case, the tribunals at both First and Upper Tier had found for Ms Adams' company. ICAS also reported on this case and the article written at that time contains more detail as to the intricacies of those two tiers.

The previous two successes counted for very little at the Court of Appeal. The stance taken by the judiciary in this hearing was to go back to basics and examine three principles established in the Ready Mixed Concrete case: (i) mutuality of obligation, (ii) control, and if these are both found to be present, (iii) whether the other elements of the relationship amount to a contract of service.

One of the key errors the Court of Appeal found in the two Tribunals' judgements had been that they did not look at each of Kaye Adams' contracts separately. Had they done so, they would surely have concluded that the contract with the BBC (which the case was founded upon) was one of employment.

Despite these findings, however, the Court of Appeal then sent the case back to the Tribunal for further consideration of application of what it opines to be the correct test, and for appropriate extensions to obtain missing facts.

The judge gave away what could be taken to be an element of frustration in the different methodologies used by courts and tribunals to decide on employment status cases. He said, "it might be supposed that, and it would certainly be desirable if, there were one clear test or approach to determining whether a person was an employee". The judgement made it clear that a person's employment status should not be open to interpretation by subjective application of different, potentially conflicting, tests – saying that this is "intolerable".

Conclusion

It would certainly save time, money, and a lot of work on both sides if this were to be the situation going forward, and fewer cases would likely end up at the Tax Tribunal in the first place as there would be more certainty in the decision-making process.

If you wish to contribute to the debate…why not contact the ICAS tax team at tax@icas.com.

Or consider helping the tax department in its policy work by joining a tax committee as a volunteer.

FRC ISSUES GUIDANCE ON PROFESSIONAL JUDGEMENT

The Financial Reporting Council (FRC) has published professional judgement guidance for auditors to improve how they exercise professional judgement. The new guidance includes a framework for making professional judgements and a series of illustrative examples. The guidance will be of particular use for auditors and central technical teams, but will also have wider interest for those interested in audit quality, such as audit committee members and investors.

The guidance is non-authoritative; it is intended to be persuasive rather than prescriptive, encapsulating good practice. However, practitioners who chose not to use or consider this guidance will need to be prepared to explain how they have complied with the relevant engagement standards.

Firms who already have a professional judgement framework are not required to adopt the FRC's instead. However, the FRC would expect those firms to analyse and understand the FRC's Framework and identify and remedy any areas where their own frameworks could be enhanced. The FRC would also encourage those firms to assess how and in what circumstances they apply their frameworks.

They believe that the process for implementing the new Quality Management Standards (ISQM (UK) 1, ISQM (UK) 2 and ISA (UK) 220) represents a significant opportunity to ensure that any professional judgement framework that is being applied helps address risks to audit quality within the firm. The FRC also encourages those firms who do not yet have their own professional judgement framework to consider the merits of developing one, or applying the FRC's. Crucially, it is not simply the existence of a framework which is important, but how effectively it is used in the specific circumstances of a firm, or of an engagement.

The framework, when applied by individual practitioners, is intended to enhance the quality and consistency of the exercise of professional judgement in two ways:

- Understanding the nature of a more structured approach can help individuals and teams improve their more intuitive judgement-making, for example by deepening their understanding of areas where they may be most susceptible to biases and other judgement traps.
- Where a more structured approach is appropriate, the framework can help auditors take account of all relevant considerations and achieve a high quality of judgement.

The framework consists of four main components which are broken down into a series of sub-components as follows:

1. Mindset

An appropriate mindset for auditors exercising professional judgement.

Sub-components

(i) Appreciation of the purpose of audit and its public interest benefits

(ii) Professional Scepticism

(iii) Understanding of biases and other relevant psychological factors

(iv) Sensitivity to uncertainty

(v) Commitment to quality

2. Professional Judgement Trigger and Process

A suggested professional judgement process, together with a reminder to remain alert to situations which may require professional judgement.

Sub-components

(i) Remain alert to situations which require the exercise of professional judgement

(ii) Consider who is the right person to make this judgement

(iii) Appropriately frame the issue

(iv) Marshal your information

(v) Conduct the analysis

(vi) Stand back, and conclude

(vii) Document, communicate and reflect

3. Consultation

Effective communication with a range of relevant parties.

4. Environmental Factors

Factors that may be present in the environment of those making a judgement which can impact on how challenging it is to exercise professional judgement in an appropriate manner.

Sub-components

(i) Audit firm: culture, resources, training, and processes

(ii) Quantity and quality of relevant information available

(iii) Time and resources available

(iv) Audited entity: management and those charged with governance

The framework and illustrative examples are also available as standalone documents. The illustrative examples illustrate application of the framework in a range of scenarios.

The FRC has also published an expectations paper which outlines its expectations in relation to the guidance. This highlights that, as stated above, the Framework is intended to have the status of non-prescriptive guidance which is consistent with a range of other guidance (Practice Notes for example) which:

"are persuasive rather than prescriptive and are indicative of good practice…. Auditors should be aware of and consider Practice Notes applicable to the engagement. Auditors who do not consider and apply the guidance included in a relevant Practice Note should be prepared to explain how the engagement standards have been complied with."

Practitioners are therefore expected to be aware of guidance that the FRC issues and to consider its relevance to audit and assurance engagements. The FRC's intent is that:

- It can be applied at a firm-wide level, and potentially incorporated into the firm's methodology;
- It may be an important consideration in the development of a Quality Management System in accordance with ISQM (UK) 1;
- It can also be applied in the circumstances of an individual audit engagement as a stand-alone guide to the application of professional judgement;
- It can be used by individual practitioners at any level of seniority in the conduct of an audit or assurance engagement, and provides high level principles and a benchmark for the application of professional judgement.

The Framework sets out principles that can be applied to help deliver high quality professional judgement, an indicative process to follow, risks and mindset traps, and illustrative examples. Any of these aspects of the material can be applied in a variety of circumstances – and indeed prescription might be impracticable or have outcomes which are inconsistent with the FRC's objectives. The FRC's intent is not to create unnecessary process or documentation, but to enable better and more consistent professional judgement. The FRC highlights that it is important to note that although the Framework itself is non-prescriptive, the application of professional judgement in the conduct of audits (and other assurance engagements) is a requirement of the auditing standards.

In terms of applying a Professional Judgement Framework, in practice there is currently divergent practice with some firms focussing on central methodology and/or training applications, and others focussing instead on more complex and subjective professional judgements made at the engagement level. The FRC believes that it is a matter for audit firms to decide which approach will be more effective in their individual circumstances. It is that assessment of how a framework can drive better and more consistent professional judgements that is critical, and how it can (or could) help manage risks to quality management. Audit firms will therefore need to understand what additional opportunities there are to ensure that a professional judgement framework is understood and socialised within the firm, and that appropriate expectations are set for how it can be used.

NO RECORDS? PAYE & PENALTIES APPLY

This article explains why an employer who did not keep proper records had to pay PAYE arrears and penalties for failure to make PAYE returns even though no PAYE would otherwise have been due. Do you have clients like this?

This tax case, known as the Hedges case, which was heard at the First Tier Tribunal in November 2021, the decision having been handed down in March 2022, is not a big hitter in terms of money. In fact, the amounts claimed as due by HMRC in PAYE and penalties amounted to less than £16,000.

However, it is not money that matters here – it is the principle, and the often-underestimated power of the PAYE Regulations. Generally speaking, the PAYE

Regs are particularly good at placing the burden firmly in the employer's lap when it comes to not only operating a payroll, but also proving that they have carried out the right processes when it comes to operating PAYE. The Employer's Further Guide to PAYE sometimes fails in its use of simplistic language to convey the serious nature of the record-keeping requirements - and attention must therefore be paid to every subtlety.

In this case, none of the employees concerned earned enough to pay any PAYE. So how did the employer end up getting their knuckles rapped and presented with a bill for 4 years' PAYE arrears and penalties?

Background

The Farmhouse public house in South London found itself under the scrutiny of an employer compliance review whereby the compliance officer discovered that Hedges, who was the manager and lessee of the pub, had been employing staff without maintaining the required standard of records as described in the Employer's Further Guide to PAYE. What was he doing wrong?

The compliance officer established that although the employees did not technically earn enough in that employment to suffer PAYE deductions from their pay, the pre-employment checks including starter checklists which should have been completed by the employer were absent, as was any form of Real Time Information record-keeping. As such, it would not have been possible for Hedges to prove that he had made the necessary checks to determine whether the employees were earning income from other sources and potentially using up their UK Personal Allowances elsewhere.

Cardinal rule – back to basics!

As payroll and employment taxation professionals know, the cardinal rule on commencement of employment is to establish this fact pattern. The default position is then to operate BR tax codes (or if they are a higher rate taxpayer, DO) on any new employee who cannot declare the employment they are about to commence is their only or main job in accordance with the starter checklist.

It is vital that employers get this first step right – to ensure that the employee is paying the right amount of tax at the right time. HMRC reserves the right to charge PAYE arrears on this basis alone.

Half cocked

The FTT found the facts showed "that there was a PAYE scheme set up in relation to Mr Dean Hedges' employees at the Farmhouse pub, which operated from 6 April 2013 to 1 November 2013 and that 7 months of nil returns were made. At this point, the scheme was cancelled".

Hedges argued that he had been instructed by HMRC to discontinue the PAYE scheme – but his record keeping was unable to prove this. It appears, when reading between the lines, that Hedges had simply decided to stop operating the scheme because no-one was paying any taxes, so to him, it was simply a superfluous administrative exercise. Unfortunately, this meant that he was not adhering to the PAYE Regulations and had inadvertently tripped himself up.

HMRC's stance – using the available legislation to collect tax and impose penalties

The Tax

HMRC issued Regulation 80 Determinations under the Income Tax (PAYE) Regulations 2003 (SI 2003/2682). Regulation 80 applies if "it appears to HMRC that there may be tax payable for a tax year" under Regulation 67G or 68, which both require employers to pay over amounts of PAYE deducted to HMRC.

Where it applies, HMRC can calculate the tax they deem to be due "to the best of their judgment", and service notice of their determination on the employer, which is given legal force by Reg 80(5), which allows HMRC to compute the liability on the employer as if it was an assessment of income tax made under Sections 34 (TMA 1970) – in other words, as if the amount of tax determined was income tax charged on the employer.

Sections 34 and 36 of TMA 1970 allow HMRC to raise assessments:

(1) For any reason within 4 years from the end of the year of assessment to which it relates, and

(2) Where the loss of tax is brought about carelessly by the taxpayer, within 6 years of the end of the year of assessment to which it relates

The Penalties – PAYE returns and Real Time Information returns

Before 2015, the penalties for failing to make PAYE related returns for small employers were within the Taxes Management Act s.98A. However, Paragraph 6C of Schedule 55 to Finance Act 2009 applies, from 6 March 2015, to make a person who fails during a tax month to make a return on or before the filing date liable to a penalty of £100 for each real time information return that is not filed (where there are no more than 9 employees).

What was the Tribunal asked to do?

The FTT's task was to determine:

- Was HMRC entitled to issue regulation 80 determinations?
- Were the determinations issued according to best judgment?
- Has the taxpayer displaced the figures in the determinations?
- Did HMRC comply with the time limits for these determinations?

The FTT needed to consider whether Hedges had been careless in failing to report the payroll details required under the law in the proper manner. Due to the fact that "reasonable care" is not defined in the legislation, they referred to previous FTT cases where the concept of "reasonable care" had been a consideration, and specifically quoted Collis v HMRC [2011] UKFTT 588 (TC). This enabled them to conclude that Hedges had not taken reasonable care, which would allow HMRC to consider Reg 80 determinations.

Having established that HMRC had complied with the legislative provisions in both issuing the Reg 80 determinations and observing the time limit protocols, the FTT considered C & E Commrs v Pegasus Birds Ltd [2004] BVC 788 to determine whether HMRC had used its best judgement. They concluded that they had, albeit with some minor amendments to the computational elements in 2013 where the tax and penalties were deemed to be incorrect and revised downwards, noting that:

"The Tribunal should remember that its primary task is to find the correct amount of tax, as far as possible on the material properly available to it, the burden resting on the taxpayer. In all but very exceptional cases, that should be the focus of the hearing, and the Tribunal should not allow it to be diverted into an attack on the Commissioners' exercise of judgment at the time of the assessment."

Conclusion

Agents and employment taxes experts should be mindful of the fact that periodic discussions with employer clients who operate their own payrolls should cover off this area, and it should ideally also be considered during annual audit risk assessments and due diligence exercises under M&A processes.

It is the little things that can come back to bite you.

WRONGFUL TRADING REVISITED

The temporary suspension of the wrongful trading provisions introduced by the Corporate Insolvency and Governance Act 2020 is now a distant memory and ICAS has recently seen an increase in queries about director responsibilities when a company is in danger of trading insolvently.

It is therefore an opportune moment to revisit the wrongful trading provisions, as a reminder of the action that directors should be taking (and advising parties should be recommending that they take) to be able to demonstrate a defence to accusations of wrongful trading.

Definition

In trading conditions where the company's solvency is not in doubt, the directors are acting for the benefit of the company and its shareholders.

However, where it becomes apparent that the company is insolvent or at serious risk of insolvency, the focus of the directors' duties switches and their overriding responsibility is to act in the best interests of the creditors of the company.

If a company is insolvent and its directors know (or ought reasonably to conclude) that it cannot avoid insolvent liquidation or administration, they are under a duty to take every step a reasonably diligent person would take to minimise potential loss to the company's creditors. Failing that, they risk personal liability for any worsening of the company's financial position.

This is what is known as 'wrongful trading', as per sections 214 and 246ZB of the Insolvency Act 1986 (IA86). If a wrongful trading action is successful, the directors may be required to contribute to the company's assets.

Fraudulent trading

Wrongful trading should not be confused with fraudulent trading – its more serious cousin.

Fraudulent trading is a criminal, as opposed to civil, offence and requires intent on the part of the directors. As set out at sections 213 and 246ZA of IA86, the business of the company must have been carried on with the intent to defraud creditors of the company, or creditors of any other person, or for any fraudulent purpose.

Wrongful trading test

Wrongful trading cases remain relatively rare due to the high standard of proof required. Previous cases, such as [Re Ralls Builders Ltd (in Liquidation) [2016] EWHC 1812(Ch)] demonstrate that liability will not be imposed simply due to a company trading while in financial difficulties.

Potential for liability arises at the point that the directors know or ought to know that there is no reasonable prospect of avoiding insolvent liquidation or administration based on both the company's current position and its realistic prospects. This should be judged without the application of hindsight. What the directors ought to have concluded is assessed by reference to the knowledge, skills, and experience that a reasonably diligent person in that person's position may reasonably be expected to have, and the actual knowledge, skills, and experience that the defendant director did, in fact, have.

For example, a director who is a chartered accountant is expected to have greater skill and experience in relation to the finances of the company than a director who is a tradesman. That does not mean to say that the tradesman would not be able to be assessed on responsibility of financial decisions, just that the standard by which they may be judged may be at a lower level. There is no requirement for dishonesty by the director when it comes to assessment of wrongful trading. Further, there must have been a material increase in the company's net deficiency as regards individual unsecured creditors as a result of continued trading.

Considerations for directors

Directors of struggling companies must attempt to strike a balance between two courses of action. If they conclude that an insolvency process is required, they must start that process early enough to both protect creditors as far as possible and to avoid the risk of personal liability.

However, they must allow time to explore the options for the company's survival as exhaustively as possible. Directors' responsiveness to events will be important in determining if liability arises, as will whether their assessment of the company's prospects is ultimately considered credible. Directors should take care to gather all relevant information and continually re-evaluate their options considering professional advice and experience.

Some key considerations are:

- is the company 'insolvent', whether on:
  - a cash flow basis – i.e. it cannot pay its debts as they fall due; or
  - on a balance sheet basis – i.e. its liabilities exceed its assets.
- if the company is insolvent, is there a reasonable prospect of avoiding an insolvent liquidation or administration?
- is there funding available or arrangements that have a reasonable prospect of being agreed with stakeholders or other third parties which will prevent insolvency?

Practical steps

Some basic practical steps to consider:

- Take professional advice – from an insolvency practitioner if necessary. The advice that directors receive at the time will be of significance in assessing whether they could properly have taken the view that insolvent liquidation or administration could be averted.
- Ensure there is a paper trail evidencing all key business decisions which impact creditors. It is vitally important that all decision-making is fully documented.
- Back up with financial information and forecasts. Cashflow forecasts should focus on the medium to longer term backed up by separate short-term forecasts where the cashflow situation is more critical. Stress test the assumptions made within the financial forecasts to ensure that they are realistic to be achieved.
- Discuss with stakeholders where this is appropriate. There should be a clear understanding of attitudes of stakeholders and the impact that this might have on the business. It is particularly important to consider for instance the attitudes of banks and other finance providers, key suppliers as well as equity shareholders in the business.
- Regular board meetings should be held, and documented, to continually assess the viability of the business.

HAVE THE 'OFF-PAYROLL' WORKING REFORMS WORKED?

The Public Accounts Committee (PAC) report published on 25 May 2022 makes interesting reading for anyone involved in the world of off-payroll working (OPW). The underlying question being asked is: is the instability of the off-payroll working regime as it currently stands, with all the uncertainty and unintended consequences it brings, proportionate to the additional revenue raised?

Taking several key observations and recommendations of the report, in turn, we learn that:

Off-payroll implementation issues

The PAC noted that there were high levels of non-compliance in central government, which could only reflect poor implementation by HMRC and other government bodies. The recommendation was that HMRC should produce sound statistics illustrating the key areas of public sector non-compliance to allow for the development of solutions to curb these instances. Two "quick wins" in the form of improvement of existing guidance and tools were suggested.

The PAC also wished to be provided with a further update 'on how the private sector reforms are being implemented in six months' time.

The 'offsetting' problem – double taxation for some?

The report also provides situations in which individuals have been taxed twice, or not at all, and instances of the wrong party becoming liable for the tax.

The Employment Status & Intermediaries Forum (formerly the IR35 Forum) members raised this issue in 2018 as a widespread problem facing engagers and contractors and highlighted its inherent unfairness, suggesting that a 'Demibourne' style solution could be utilised by HMRC to ensure the right person paid the right tax at the right time. The group considered that: Notifying the PSC/worker that a refund of tax may be due (as HMRC currently propose) results in the wrong party benefiting from the arrangement and thus creates an unjust result, as follows:

a) The business/agency bears the full PAYE/NIC.

b) Both PSC and worker ultimately receive tax-free earnings regardless of whether reasonable care was taken in issuing the Status Determination Statement (SDS).

c) Once this perverse effect becomes known in the sector, it could potentially trigger claims from workers/PSCs that they have been mis-categorised as outside OPW to trigger a tax windfall in their favour.

d) By notifying the PSC/worker, the group opined that HMRC would effectively be breaching the fee-payer's confidentiality – however, HMRC disagreed with this point.

In the summer of 2021, after gaining very little ground, the non-HMRC Forum members wrote to the Financial Secretary to the Treasury, Rt. Hon. Lucy Frazer QC MP, to ask her to intervene and push for a resolution. Currently, the Forum is working with HMRC policy to find a practical and fair workaround which gives a similar outcome to 'Demibourne' protocols and hopefully a resolution will be reached in the autumn or winter of 2022/23.

Structural problems

In spite of the taxation of intermediaries concept which is set out in Chapter 8 of ITEPA 2003 having been introduced over 22 years ago, various additions were made to it in the process such as the Managed Service Companies legislation in Chapter 9 of ITEPA and the Off-Payroll reforms set out at Chapter 10 of ITEPA, the PAC found that there are still ongoing structural issues in terms of how the legislative provisions translate into practical operation.

The PAC considered that HMRC should be making more effort to review how the legislation is working in practice and identify efficiencies. They observed that particular emphasis could be placed on obtaining the right kind of data which might assist them in quickly identifying non-compliance cases and eradicate cases where the same income is being taxed twice or that the wrong person is paying the tax (i.e., the offsetting problem mentioned above).

CEST Tool

The PAC highlighted the ongoing problem that the widely criticised CEST Tool has not been able to produce a determination in a large number of cases.

Challenging status determinations

The report concludes that it is too difficult for workers to challenge incorrect status determinations, which places them at a significant disadvantage in the

process. They recommended that HMRC must facilitate an expedited and independent dispute resolution process – something which HMRC stepped away from when these reforms were introduced, saying that any disputes were a matter for the contractor and engager to resolve. They also recommended that HMRC should understand the level of appeals currently in progress and whether these are working as they should.

Disproportionate effect on different sectors

The PAC expressed no confidence that HMRC has performed any exercises to understand whether any sector has been disproportionately affected by the reforms, and the reasons for any adverse outcomes. They recommended that HMRC should 'proactively identify and work with sectors that have been particularly affected to understand the challenges, establish how to address them and make it easier to comply'.

The PAC requested that HMRC should report back on this in 6 months' time.

Impact assessment

The PAC requested that HMRC should work up a comprehensive cost-benefit analysis which it should present to Parliament, setting out the costs of compliance to HMRC itself, as this has not been done and there is therefore no information on what the actual cost has been to implement the reforms.

Wider impact of the reforms

The report noted that HMRC has not done enough work to fully understand the wider impact of the reforms introduced on workers/contractors, employment opportunities and labour markets, and whether the legislative provisions are being applied in practice as per the original intentions of the measures. The PAC recommended that HMRC conduct and publish its research into this.

Private sector impact distorted by Brexit and Covid

Finally, the PAC perceive that Brexit and Covid have played a significant part in distorting the impact of off-payroll working reform and the costs associated with its implementation to the public and private sectors as well as to HMRC itself.

So, will anyone ever get to the bottom of the proportionality point?

Clearly, there is still a long way to go before we have a system which is working in practice whilst raising the right amount of revenue from the right people at the right time.

UPDATE TO THE MONEY LAUNDERING REGULATIONS

Draft legislation for the introduction of The Money Laundering and Terrorist Financing (Amendment) (No.2) Regulations 2022 ('the regulations') has now been laid in parliament

These regulations update the existing UK anti-money laundering legislation by making some time sensitive updates to The Money Laundering Financing and Transfer of Funds (Information on the Payer) Regulations 2017 ('the MLRs'). The changes are being made to ensure that the UK continues to meet international standards on anti-money laundering and counter-terrorist financing whilst also strengthening and clarifying how the UK's AML regime operates, following feedback from industry and supervisors.

The main changes, most applicable to firms, are outlined below.

Trust and Company Service Provider services and business relationships

Effective 1 September 2022, Regulation 4 widens the meaning of a trust or company service provider ('TCSP') by amending regulation 12 of the MLRs to include the formation of all forms of business arrangement, not just companies and legal persons. By extending this to the formation of a 'firm', which is defined in regulation 3 of the MLRs, it will now specifically include Limited Partnerships which are registered in England and Wales or Northern Ireland (Scottish Limited Partnerships are already included as they are "legal persons" which are caught under the current provisions). The amendment regulation will cover all business arrangements and services provided that are required to be registered with Companies House.

An amendment is also being made to regulation 4 of the MLRs so that TCSPs are required to conduct customer due diligence ('CDD') when they are providing services outlined in regulation 12(2)(a), (b) and (d).

Discrepancy Reporting

Effective 1 April 2023, Regulation 9 amends regulation 30A(1) of the MLRs to extend the scope of the discrepancy reporting regime so that it is an ongoing requirement and limiting the requirement to report only 'material discrepancies'. Regulation 30A of the MLRs requires relevant persons to report to the Registrar of Companies any discrepancies between the information they hold about the beneficial owners of companies, as a result of CDD measures, and the information recorded by Companies House on the public companies register. The requirement applies at the onboarding stage, "before establishing a business relationship" therefore the amendment aims to enhance the accuracy and integrity of the register by making the obligation ongoing.

Suspicious Activity Reports

Effective 1 September 2022, Regulation 13 makes it clear that supervisory authorities can directly require members to show them Suspicious Activity Reports ('SARs') "to help them in fulfilling their supervisory functions and driving greater consistency of approach to utilising SARs across supervisors".

The amendments introduce an explicit legal right for supervisory authorities to access, view and consider the quality of the content is SARs submitted by supervised populations. This access will help supervisors deliver more effective training and clear feedback on the quality of SARs. At present, there is no standardised approach to accessing SARs due to the ambiguity of the MLRs.

TOMORROW'S PRACTICE – THE IMPACT OF BASIS PERIOD REFORM & MTD FOR INCOME TAX

Change is on the horizon for unincorporated businesses and their advisers. Basis period reform and Making Tax Digital for income tax (MTD ITSA) are the biggest changes to income tax administration since the roll out of self-assessment in 1996. What is the impact and how can firms prepare?

Basis period reform for trading income for unincorporated business is an opportunity for firms to engage with their small business clients. It undoubtedly will result in some additional advisory and tax planning opportunities. It will be important for practices to explain the value of the additional work and look beyond necessary compliance service.

What is the impact?

Basis period reform impacts all unincorporated business which do not have a 31 March/5 April accounting year end. The impact will be particularly significant for businesses with a year-end early in the tax year.

The impact is both administrative, affecting timescale for preparation of accounts and submission of return, and financial, as tax will be payable nearer to real-time. There will also be a 'catch-up' tax bill on additional profits for many in the move to tax year basis of assessment.

When taken alongside Making Tax Digital for income tax (MTD ITSA) quarterly reporting, it is likely to result in increased concentration of workloads within firms. This will increase resourcing demands and may also result in increased costs for clients.

Pressure on resources

What does this look like on practices? A key impact is that accounts will be needed sooner as submission date for tax returns moves closer to real time. MTD ITSA quarterly reporting also means providing data to HMRC earlier.

Consider a business with a 30 June accounting date. Basis period reform and MTD ITSA will mean that the following accounts will be needed:

- 30 June 2022 accounts: needed for filing ITSA return for 2022-23 by 31 January 2024
- 30 June 2023 and 30 June 2024 accounts, needed to finalise taxable profit for the transition year of 2023-24, by 31 January 2025
- Quarter to 30 June 2024: under MTD quarterly reporting, needs to be submitted by 5 August 2024

In the period January 2024 to January 2025 this means that potentially three years accounts need to be finalised.

In addition to the workload, there are decisions and choices. Should businesses change their accounting year end to 31 March to avoid the need to apportion

profits to match the tax year? And if so, when should the change be made?

There is also the impact on tax bills to consider. What will the impact be on tax bills for 2023-24 onwards and how can this be mitigated?

Spreading relief and overlap relief may help reduce the impact of higher transition year profits, but their availability depends on timing, business history and an individual's specific circumstances.

ICAS practice briefing

ICAS has prepared a briefing to help inform decisions: Tomorrow's practice - the impact of basis period reform and MTD for income tax. The briefing provides worked examples and reviews the options available to businesses and firms.

HMRC & TAX UPDATES

HMRC service standards – joint letter from ICAS and other Professional Bodies

ICAS and other professional bodies (CIOT, ICAEW and ATT) wrote to HMRC on 15 June raising issues with service levels and the agent dedicated line ('ADL'). The letter also requested some other specific actions.

On the ADL the letter noted that feedback indicates that performance appears to be erratic; there are sometimes exceptionally long waiting times, and calls can be cut off unexpectedly and promised call backs do not happen. Members are also concerned that helpline hours have not been restored to pre-pandemic levels.

HMRC replied in July. On performance and the ADL, the response comments:

"In terms of our performance, we made solid progress in 21/22 and this will continue in 2022/23.

"We aim to answer all calls to the ADL within 10 minutes and our data shows that we rarely exceed this. If any agents are facing specific problems, then I would appreciate a bit more information so that we can investigate what has gone wrong.

"We are reviewing the ADL position, ahead of a bespoke RBSG to discuss this over the next few weeks.
"In terms of our other tax lines, our average call wait times (year-to-date) have fallen by seven minutes between April 2021 to February 2022 and we are continuing to improve these services, by recruiting and training extra staff.
"We have also increased the proportion of correspondence cleared within 15 days by more than 20 percentage points between April 2021 and February 2022. Our overall customer satisfaction has remained above 80 per cent but we know that there are areas we need to renew our focus to make sure our service levels are where they it should be."

In view of the comments about specific problems with the ADL, we would welcome further feedback from Members about their experience with ADL call answering times – email tax@icas.com to provide input.

HMRC Service Dashboard – now available on GOV.UK

One of the specific actions requested in the joint letter to HMRC was a timeframe for the full rollout of the HMRC Service Dashboard (intended for agents) and the improved 'Where's My Reply' service.

In a helpful development, following the response to the joint letter, the service dashboard has been moved out of the testing phase (when access was via the agent online forum) and is now available on GOV.UK. The improved 'Where's My Reply' is also now available. These tools allow agents and taxpayers to see how long they can expect it to take for HMRC to deal with several types of correspondence, returns, claims etc.

Whilst the increased transparency is welcome, the dashboard shows that in some areas there continue to be significant delays. The dashboard is also not comprehensive – we have received reports from Members about areas not included in the dashboard. ICAS will continue to raise feedback from Members on problems they encounter, at meetings with HMRC and through the agent online forum. Members may wish to consider joining the forum, if they are not already members. Please email tax@icas.com with any feedback on the dashboard.

Charter Annual Report – ICAS input through the Charter Stakeholder group

HMRC is required to publish an annual report setting out the extent to which it has demonstrated the standards of behaviour and values included in the HMRC Charter.

The Charter Stakeholder group (CSG) is made up of representatives of the tax community, including ICAS, ICAEW and the CIOT. It holds regular meetings with HMRC to discuss how the Charter is being reflected in taxpayer and agent experience of dealing with HMRC. It also gives formal input about HMRC's performance, for inclusion in the annual report.

The 2022 report, covering the period April 2021 to March 2022, was published on 18 July. The CSG input to the report included an overview in the main report and comments on the individual Charter standards in Appendix 3. The overview noted that the group considered that HMRC had generally performed well in delivering the COVID-19 support schemes and implementing processes for the UK's exit from the EU. However, negative feedback from members of the bodies making up the CSG had increased considerably, with some common themes. Two principal areas of concern were highlighted: customer service levels and lack of consequences for HMRC failure.

Continued overleaf….

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In his opening message, the Chief Executive and Permanent secretary for HMRC, Jim Harra acknowledged that the decisions made about prioritising work during the pandemic meant that customer service levels fell below where HMRC wanted them to be for most of the year. This caused frustrations and difficulties for agents and taxpayers, and he pointed to the comments of the CSG that customer service was their greatest concern over the period.

We welcome feedback on HMRC's performance against the Charter Standards, to raise at CSG meetings: email tax@icas.com to share your comments.

Overlap relief - obtaining details from HMRC

ICAS has been asked whether HMRC has a process for providing details of overlap relief to agents ahead of the basis period transition year. In evidence to the House of Lords Economic Affairs Finance Bill sub-committee last year, HMRC said they were looking at how to get the information to taxpayers: see the answers to Questions 64, 68 and 69.

We raised this with HMRC in June to find out if they now have any definite plans for how they might provide the information – to taxpayers and agents. We received the response below – clearly no decision has been reached yet. We have asked whether they have any idea when they might be able to make an announcement, as we anticipate that the question will keep being raised ahead of the transitional period.

Response from HMRC:

"*Currently, we are still exploring the feasibility of providing overlap relief details to taxpayers and potentially agents as part of our work on implementing basis period reform. This includes looking at the feasibility of providing figures of overlap relief that have previously been included in tax returns, as well as the feasibility of carrying out more complex reconstructions of overlap relief figures from information included in previous tax returns. As part of this process we are looking at a wide range of options using different communications methods and exploring whether it is possible to provide certain information directly to tax agents.*

In the government's response to recommendation 2 of the House of Lords Finance Bill Sub-Committee's report on basis period reform and uncertain tax treatment, we set out a written response covering overlap relief; you will be able to find this here'.

Access to HMRC digital services - addition of Great Britain (GB) driving licences as evidence

ICAS and other professional bodies have been receiving reports about difficulties encountered by agents (and taxpayers) in setting up or renewing access to HMRC digital services because of the limited list of items accepted as evidence of identity. Whilst NI driving licences were included on the list, GB driving licences were not.

On 30 June, HMRC confirmed that they had added GB driving licences as an extra evidence source – to help more 'customers' to get online to use their digital services.

HMRC noted that they need two forms of evidence to confirm identity online – two of the items on the following list can now be selected where they are available: tax credit claim details; P60 or most recent payslips; UK passport details; information held on credit file (such as loans, credit cards or mortgages); a Self-Assessment tax return (in the last 3 years) and/or a GB driving licence (DVLA-issued) or NI driving licence (DVA-issued).

Euro Pacific Bank - HMRC checking UK taxpayers

Information provided by HMRC:

HMRC is part of the Joint Chiefs of Global Tax Enforcement, known as the J5, which comprises leaders of tax enforcement authorities from Australia, Canada, the UK, US, and the Netherlands.

Puerto Rico's Office of the Commissioner of Financial Institutions (OCIF) announced on 30 June 2022 that it had issued a Cease and Desist order to Euro Pacific Bank, for non-compliance with Puerto Rican regulations. The bank had previously been subject to a day of action through the Joint Chiefs of J5 in 2020, which was aimed at tackling suspected tax evasion and money laundering.

HMRC are checking details of hundreds of UK taxpayers to see if accounts have been properly disclosed. A number of investigations have been opened already, with more planned. HMRC are planning a nudge campaign to commence in August 2022. Anyone needing to correct their tax affairs should come forward and disclose through the Worldwide Disclosure Facility.

There is more information in a J5 Media Release. HMRC also posted on Twitter and LinkedIn.

Time to take National Minimum Wage seriously

The 2022 Ask ICAS NMW Webinar

ICAS Tax's Justine Riccomini and EY's Jeni Morris presented a webinar on 26 April relating to the National Minimum Wage (NMW) and National Living Wage (NLW).

The webinar was an informal, fireside chat around the key issues which NMW is currently throwing up for employers and agents. The webinar has received excellent feedback from delegates on the basis of its style and content, which demonstrated how risky NMW can be for employers – and of course, the consequences of getting it wrong impacts on both employers and agents.

The main topics covered in the discussion were:

- Understanding the NMW and who it applies to
- Getting it wrong – a costly business
- Some recent naming and shaming – what did they do wrong?
- Navigating NMW – key areas of interest for NMW Compliance
- Amended regulations in 2020 – what has changed?
- What is the Single Enforcement Body and what does it mean for me and my clients?

ICAS is keen for its members to understand the pitfalls associated with National Minimum Wage Compliance. It is an area which all members operating outsourced payrolls and their employer clients need to be alert to. Some key areas include mergers and acquisitions, paying the Living Wage, and higher rate earners – how can an employer fall foul of NMW?

The webinar is available to watch on demand now. Copies of the slides and the Q&A are also available on the same page.

ICAS calls for a UK strategy to support the transition to net zero

ICAS has issued a briefing paper 'The role of tax in getting to net zero', discussing how tax can be a vital part of the package of measures needed to deliver the UK's ambitious target for reducing emissions.

ICAS would like to see the Government issue an environmental tax roadmap or strategy. In the absence of such a roadmap, individuals and businesses are likely to find it difficult to plan ahead for the tax changes and costs which will arise as part of the implementation of the Net Zero Strategy. It may also be difficult for the Government to ensure that tax policy is closely aligned with the development of new green technologies and supporting infrastructure.

Making Tax Digital reminder for VAT customers

Regardless of taxable turnover, businesses now need to keep digital records, sign up for MTD and file all their future VAT returns using MTD-compatible software.

It is hoped this will reduce common mistakes and make it quicker and easier for clients to manage their tax affairs.

Find out what actions businesses need to take now and help and support for MTD on GOV.UK.

PAYE tax refund – using the HMRC app

Taxpayers can quickly check and claim a PAYE tax refund using the HMRC app.

The app is a free, quick, and secure way to claim a refund that will paid directly into the taxpayer's bank account.

An animation is available on YouTube highlighting key features as well as how to claim a tax refund.

COMPANIES HOUSE UPDATES

Companies House – closure of public counters

In response to the coronavirus (COVID-19) pandemic, Companies House public counters in Cardiff, London, Belfast, and Edinburgh offices were closed. Companies House has now decided to not re-open the public counters, including the London office.

More customers are now using their online services to file accounts, confirmation statements, mortgage documents, start or remove a company.

The upload service can also be used to file a range of documents online that would previously have been sent in paper format. In this service, you can upload documents for:

- Share capital
- Registrar's powers
- Change of constitution
- Scottish limited partnerships
- Scottish qualifying partnerships
- Insolvency (registered insolvency practitioners only)

Filing LLP accounts - update

Companies House has added a section to its filing guidance for UK registered limited liability partnerships (LLPs) on filing a strategic report.

The guidance sets out the preparing and filing requirements for all UK registered LLPs and was updated to include the Energy and carbon report and the Strategic report.

Electronic same day services available

The following same day services are available:

- Change of company name
- Incorporate a company
- Upload a reduction of capital (form SH19)
- Order certified copies of certificates and documents held on the register

TECHNICAL BULLETIN

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