



HM Revenue
& Customs

Protecting your taxes in insolvency

Consultation document

Publication date: 26 February 2019

Closing date for comments: 27 May 2019

Subject of this consultation:	Protecting your taxes in insolvency
Scope of this consultation:	<p>The government announced at Autumn Budget 2018 that it will introduce legislation in Finance Bill 2019-20 to make HMRC a secondary preferential creditor for taxes paid by employees and customers.</p> <p>This measure would protect the payment of tax debts for PAYE (including student loan repayments), NIC (employee contributions only), CIS and VAT that are due at the commencement of the insolvency.</p>
Who should read this:	This consultation will be of interest to individuals, shareholders, directors, lenders, companies and insolvency practitioners, as well as their advisors and agents.
Duration:	The consultation runs for 12 weeks, starting on 26 February 2019 and ending on 27 May 2019.
Lead official:	Ade Adetosoye, Steve Taccagni, HM Revenue & Customs
How to respond or enquire about this consultation:	Responses and general queries about the content or scope of the consultation can be sent by email to insolvency.protectingtaxes@hmrc.gsi.gov.uk or by post to: HMRC – Debt Strategy, 7th Floor, 10 South Colonnade, Canary Wharf, London, E14 4PU.
Additional ways to be involved:	HMRC will be happy to hold meetings with interested parties to discuss the proposals.
After the consultation:	The government will publish a summary of the responses along with draft legislation in summer 2019.
Getting to this stage:	<p>Prior to 2003, HMRC was a preferential creditor for certain taxes, but the Enterprise Act 2002 reduced our status to that of non-preferential creditor for all forms of tax.</p> <p>HMRC has continued to be a non-preferential creditor since 2003 and losses to the exchequer from insolvency have increased.</p> <p>The government decided that from April 2020 certain tax debts should be protected in an insolvency because they are taxes that have been paid by employees and customers and being held by the business on behalf of HMRC.</p>
Previous engagement:	This is the first public consultation on the issue by HMRC.

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1. Introduction

Background

- 1.1 At Budget 2018, the government announced that it will introduce legislation in Finance Bill 2019-20 to make HMRC a secondary preferential creditor for certain tax debts paid by employees and customers.
- 1.2 This consultation sets out how HMRC proposes to implement the change. We are seeking views from interested parties, particularly those who will be affected by these changes, including businesses, lenders, insolvency practitioners, advisors and representative bodies, to ensure that this change is implemented in the most effective way.

What is the change?

- 1.3 Taxes paid by employees and customers do not always go to funding public services, if the business temporarily holding that money goes into insolvency before passing the tax on to HMRC. Instead, they often go towards paying off debts to other creditors.
- 1.4 The government has decided that when a business enters insolvency, more of the taxes paid in good faith by its employees and customers should go to fund public services as intended, rather than being distributed to other creditors, such as financial institutions. The new rules will come into force for insolvencies that commence from 6 April 2020.
- 1.6 This measure will amend Insolvency legislation to move HMRC up the creditor hierarchy for the distribution of assets in the event of insolvency, but only for taxes held by a business (this include individuals and partnerships) on behalf of their customers and employees.
- 1.7 This change will enable a larger proportion of those taxes that have been paid to fund public services be used as intended.
- 1.8 The change applies to certain tax debts paid by employees and customers - VAT, PAYE (including student loan repayments), Employee NICs and Construction Industry Scheme Deductions. HMRC will remain an unsecured creditor for taxes directly on businesses, such as Corporation Tax and Employer NICs.

2. Existing rules

What is the current order of asset distribution in insolvency?

2.1 The current order of distribution is set out in the Insolvency Act 1986 and the 2016 Rules.

Broadly, asset realisations are paid out in the following order:

- Secured creditors with a fixed charge (after costs of realisation)
- Insolvency practitioners' fees and expenses
- Preferential unsecured creditors
- Prescribed part creditors
- Secured creditors with a floating charge
- Non-preferential unsecured creditors
- Shareholders or individual"

Secured creditors with a fixed charge: Fixed charge holders are often banks and other asset-based lenders who hold security over a specific asset. When a fixed charge is provided to the lender, the borrower loses the right to sell or trade the item, which might include property, plant, machinery and vehicles.

Insolvency practitioners' fees and expenses: The insolvency practitioner's remuneration, and costs of administering the process. Costs and expenses can be incurred when realising assets, distributing funds, providing accounts and reports, and investigating the conduct of directors.

Preferential unsecured creditors: These are split into two classes.

Ordinary preferential creditors include employees entitled to arrears of wages, holiday pay, and other statutory payments up to a certain limit. This also includes deposits that fall within the Financial Services Compensation Scheme ("FSCS").

Secondary preferential creditors Secondary preferential creditors are only paid once ordinary preferential creditors are paid. They include currently, in brief, those parts of a deposit which do not fall within the protection of the FSCS.

Prescribed part creditors: The law "ring-fences" a fund that is used by the insolvency officer holder to pay a dividend to non-preferential unsecured creditors. The Prescribed Part is calculated as 50% of the first £10,000

available and 20% thereafter up to a maximum of £600,000. There is a [separate proposal](#) to raise this cap.

Secured creditors with a floating charge: Assets subject to a floating charge often include stock, raw materials, work-in-progress, fixtures and fittings – basically any other assets not subject to a fixed charge. Assets of this type can be traded in the normal course of business.

Non-preferential unsecured creditors: These include trade creditors, suppliers, customers, contractors, and some staff claims. Currently all tax claims are non-preferential unsecured debts and so have no special priority over other debts, despite the fact the taxes were intended to be held temporarily before being paid into the exchequer.

Shareholders or individual: In a company insolvency, shareholders are the final group to be paid. Because they have taken a business risk in providing money to the company, they are not entitled to a distribution until all other creditor groups have been paid.

- 2.2 Each class of creditor must be paid in full before the insolvency officer holder can distribute funds to the next group. It is intended that HMRC will become a secondary preferential creditor for taxes paid by employees and customers (as per paragraph 1.8) when this measure is implemented.

3. Scope of proposals

HMRC debt management approach

- 3.1 The majority of people in the UK want to pay the right tax at the right time because they believe that it is the right thing to do and appreciate that tax revenue funds public services for everyone. HMRC provides a flexible range of support for those who would like to pay on time, but find it hard to do so.
- 3.2 We will continue to support viable businesses with our Time to Pay (TTP) arrangements. It's essential that any business that is struggling to pay what they owe contacts HMRC, with support available through the [Business Payment Support Service](#).

What does this proposal do?

- 3.3 For all formal insolvencies that commences after 6 April 2020, HMRC will move up the creditor hierarchy for the distribution of assets with respect to certain taxes held by any insolvent entity.
- 3.4 The legislation in the Finance Bill will apply to England, Wales and Scotland. For Scotland, a legislative consent motion may be required.

Secondary preferential creditor

- 3.5 HMRC will become a secondary preferential creditor for the specific taxes paid to a business by employees and customers, and any interest or penalties arising from such debts.
- 3.6 This means HMRC will move ahead of holders of floating charges (mainly financial institutions) and other non-preferential unsecured creditors, but remain below holders of fixed charges (also primarily financial institutions) and higher-ranking preferential creditors.

Question 1: The government is committed to increasing the priority of certain tax debts in insolvency. Should they be ranked as a secondary preferential creditor, an ordinary preferential creditor, or protected in some other way in the event of an insolvency?

HMRC claims

- 3.7 This measure would give HMRC greater statutory rights in respect of the payment of tax debts for PAYE, NIC (employee contributions only), CIS and VAT that are due at the commencement of the insolvency. The payment would

be from the assets of insolvent taxpayers, above unsecured creditors and holders of floating charge.

- 3.8 The rules will remain unchanged for liabilities relating to taxes directly levied on businesses or individuals themselves, such as Income Tax, Capital Gains Tax, Corporation Tax and Employer National Insurance Contributions.
- 3.9 HMRC will continue to be a non-preferential unsecured creditor in respect of these other tax debts. As this measure only relates to employee NIC, we will separate employee debts from employer debts when submitting claims.
- 3.10 It is not proposed to introduce any time limit in respect of debts that are due. Where any of the above tax debts have not been paid to the exchequer, we consider that it should be treated preferentially, irrespective of how old the debt might be.
- 3.11 Any penalties or interest arisen from these taxes will also form part of HMRC's preferential claim.
- 3.12 The Government does not believe that these proposals would lead to particular difficulties. However, we are interested in your views on the following:

Question 2: Would any of the taxes included in this measure pose any particular challenges to insolvency office holders when they process HMRC claims?

Question 3: Do you foresee additional administrative burdens falling upon individuals, businesses or insolvency practitioners as a result of this measure? If any, how might they be lessened?

Question 4: Do you consider the objectives of any type of formal insolvency procedure will be adversely affected by this measure? If so please evidence or explain why. Please suggest how we could mitigate against this.

Transitional issues

- 3.13 This measure will have no effect in relation to any insolvency proceedings commencing before the implementation date of 6 April 2020.

Question 5: Are there any transitional issues that we need to take into consideration in implementing this measure?

Other considerations

Question 6: In your view, are there any other considerations, or other potential impacts that HMRC should take into account in implementing this measure?

4. Assessment of Impacts

Exchequer impact (£m)	2019/20	2020/21	2021/22	2022/23	2023/24	
	5	60	145	185	175	
OBR	These figures have been certified by the OBR. Further details can be found in the budget 2018 policy costing .					
Economic impact	<p>Although this change will affect financial institutions, the government does not expect it to have a material impact on lending, and the Office for Budget Responsibility made no adjustment to its forecast as a result of this measure.</p> <p>This is because:</p> <ul style="list-style-type: none"> • Financial institutions will remain above HMRC in the creditor hierarchy for fixed charges they hold over assets, and • The debts they will no longer recover are a very small fraction of total lending. Bank lending to small and medium enterprises alone was £57 billion in the 12 months to July 2018, compared to an estimated maximum yield of £185 million a year from this measure. • Other unsecured creditors – such as suppliers – are usually unable to recover any of their debts and so most will be unaffected. They currently only recover 4% of debts owed on average. <p>Where appropriate, HMRC will also continue to offer Time to Pay (TTP) arrangements to help viable businesses with tax debt avoid entering insolvency.</p>					
Impact on individuals, households and families	This proposal will have no impact on shareholders as they are only paid after all preferential and non-preferential creditors have been paid in full.					
Equalities impact	The changes are not expected to have an impact on any specific group.					
Impact on businesses and	This proposal will impact on some businesses and civil society organisations who are creditors involved in an insolvency where					

civil society organisations	HMRC is also a creditor.
Impact on HMRC or other public sector delivery organisations	This measure is being delivered through an existing IT system. The proposed changes to this system will be negligible.
Other impacts	<p><u>Competition assessment:</u> The scope of this measure has been specifically designed to ensure a level playing field for all those affected by the measure.</p> <p><u>Small firms impact test:</u> The measure may have some impact on small firms that rely on the alternative lending market for fund raising.</p>

Question 7: Do you have any comments on the assessment of equality or other impacts?

5. Summary of Consultation Questions

Question 1: The government is committed to increasing the priority of certain tax debts in insolvency. Should they be ranked as a secondary preferential creditor, an ordinary preferential creditor, or protected in some other way in the event of an insolvency?

Question 2: Would any of the taxes included in this measure pose any particular challenges to insolvency office holders when they process HMRC claims?

Question 3: Do you foresee additional administrative burdens falling upon individuals, businesses or insolvency practitioners as a result of this measure? If any, how might they be lessened?

Question 4: Do you consider the objectives of any type of formal insolvency procedure will be adversely affected by this measure? If so please evidence or explain why. Please suggest how we could mitigate against this.

Question 5: Are there any transitional issues that we need to take into consideration in implementing this measure?

Question 6: In your view, are there any other considerations, or other potential impacts that HMRC should take into account in implementing this measure?

Question 7: Do you have any comments on the assessment of equality or other impacts?

6. The Consultation Process

This consultation is being conducted in line with the Tax Consultation Framework.

There are 5 stages to tax policy development:

- Stage 1 Setting out objectives and identifying options.
- Stage 2 Determining the best option and developing a framework for implementation including detailed policy design.
- Stage 3 Drafting legislation to effect the proposed change.
- Stage 4 Implementing and monitoring the change.
- Stage 5 Reviewing and evaluating the change.

This consultation is taking place during stage 2 of the process. The purpose of the consultation is to seek views on the detailed policy design and a framework for implementation of a specific proposal, rather than to seek views on alternative proposals.

How to respond

A summary of the questions in this consultation is included at chapter 5.

Responses should be sent by 27 May 2019 by e-mail to

insolvency.protectingtaxes@hmrc.gsi.gov.uk

or by post to:

Ade Adetosoye,
HMRC – Debt Management
7th Floor
10 South Colonnade
Canary Wharf
London
E14 4PU.

Please do not send consultation responses to the Consultation Coordinator.

Paper copies of this document or copies in Welsh and alternative formats (large print, audio and Braille) may be obtained free of charge from the above address. This document can also be accessed from [HMRC's GOV.UK pages](#). All responses will be acknowledged, but it will not be possible to give substantive replies to individual representations.

When responding please say if you are a business, individual or representative body. In the case of representative bodies please provide information on the number and nature of people you represent.

Confidentiality

Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004.

If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Revenue and Customs (HMRC).

Consultation Privacy Notice

This notice sets out how we will use your personal data, and your rights. It is made under Articles 13 and/or 14 of the General Data Protection Regulation

Your Data

The data

We will process the following personal data Name/Email address/Postal address/
Job title

Purpose

The purpose(s) for which we are processing your personal data is:
Public consultation on :Protecting your taxes in insolvency

Legal basis of processing

The legal basis for processing your personal data is that the processing is necessary for the exercise of a function of a government department.

Recipients

Your personal data will not be disclosed to third parties

Retention

Your personal data will be kept by us for six years and will then be deleted.

Your Rights

- You have the right to request information about how your personal data are processed, and to request a copy of that personal data.
- You have the right to request that any inaccuracies in your personal data are rectified without delay.
- You have the right to request that any incomplete personal data are completed, including by means of a supplementary statement.
- You have the right to request that your personal data are erased if there is no longer a justification for them to be processed.
- You have the right in certain circumstances (for example, where accuracy is contested) to request that the processing of your personal data is restricted.

Complaints

If you consider that your personal data has been misused or mishandled, you may make a complaint to the Information Commissioner, who is an independent regulator. The Information Commissioner can be contacted at:

Information Commissioner's Office
Wycliffe House
Water Lane
Wilmslow
Cheshire
SK9 5AF
0303 123 1113
casework@ico.org.uk

Any complaint to the Information Commissioner is without prejudice to your right to seek redress through the courts.

Contact details

The data controller for your personal data is HM Revenue & Customs. The contact details for the data controller are:

HMRC
100 Parliament Street
Westminster
London SW1A 2BQ

The contact details for HMRC's Data Protection Officer are:

The Data Protection Officer

HM Revenue & Customs
7th Floor, 10 South Colonnade
Canary Wharf, London E14 4PU
advice.dpa@hmrc.gsi.gov.uk

Consultation Principles

This consultation is being run in accordance with the government's Consultation Principles.

The Consultation Principles are available on the Cabinet Office website:
<http://www.cabinetoffice.gov.uk/resource-library/consultation-principles-guidance>

If you have any comments or complaints about the consultation process please contact:

John Pay, Consultation Coordinator, Budget Team, HM Revenue & Customs, 100 Parliament Street, London, SW1A 2BQ.

Email: <mailto:hmrc-consultation.co-ordinator@hmrc.gsi.gov.uk>

Please do not send responses to the consultation to this address.