Security for PAYE

The recent decision in *D-Media Communications* highlights some really serious issues.

The power of HMRC to require security for PAYE and NIC is truly awesome. The principle is fair enough and we have seen it in the context of VAT for many years. Under VATA 1994 Sch 11(4), HMRC is entitled to seek security from the taxpayer if it thinks it is necessary for the protection of the revenue; for example, if the taxpayer has failed to comply with his VAT obligations or HMRC has reason to believe that he might fail to do so. This is really serious because it is a criminal offence to continue to make taxable supplies if you have not provided the security demanded by HMRC.

Of course, if a person is unable to pay his current VAT liabilities, he is hardly going to be able to pay a security representing a few months' VAT liabilities in advance. Therefore, to avoid criminal liability, he must cease to trade.

The PAYE rules for security are more recent – and are much worse. Regulation 97N of the PAYE regulations (SI 2003/2682) provides that where an officer of HMRC considers it necessary for the protection of the revenue, he may require the company, or the directors, to provide security for payment of PAYE in the future. The failure to provide security is a strict liability criminal offence, which the tribunal explained is punishable by a fine of *unlimited* amount. (I am not joking.) Ceasing to trade does not help; the criminal offence applies if you fail to pay the money. There is virtually no defence to a strict liability offence.

Fortunately, and unlike the position for VAT, there is a right of appeal against a security notice for PAYE and NICs. The tribunal is entitled to form its own view and to confirm, set aside or vary the security notice.

Having regard to the enormity of the consequences – with directors facing criminal liability and an unlimited fine for failing to provide the necessary security when the company is up to its ears in debt and has no access to funds – it is no surprise that this has ended up in court: *D-Media Communications Ltd v HMRC* [2016] UKFTT 430 (reported in *Tax Journal*, 15 July 2016).

The tribunal noted that the recipient of a notice to provide security will be criminally liable merely for the failure to provide the security. If that person simply does not have the funds, the inevitable consequence of the issue of a security notice will be that a criminal offence will be committed. No doubt influenced by the harshness of this rule, the tribunal suggested that hardship should be a factor in the decision of HMRC to require security.

The tribunal said that a policy which dictates the amount of security to be required, without regard to the ability to pay, is inconsistent with the legislation. If the taxpayer cannot pay and HMRC knows it cannot pay, then to require the taxpayer to provide security – which it would inevitably fail to do and be criminally liable – can do nothing to protect the revenue and cannot have been the purpose of parliament in making these regulations. Accordingly, the tribunal reduced the amount of the security to manageable proportions.

To make a person criminally liable for non-payment of tax is bad enough. However, to make them criminally liable for non-payment of a liability which has not yet arisen, just because HMRC is worried about it, is a very serious power indeed. It clearly deserves some control by the courts – and this case shows how badly such control is needed. ■

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FB 2016: Hybrid and other mismatch rules

A number of government amendments have been proposed to the draft hybrid mismatch rules (TIOPA 2010 Part 6A) in Finance Bill 2016.

Further amendments have been proposed to the draft hybrid mismatch rules. The key changes introduced by these amendments fundamentally impact the scope of:

- Chapter 6 (deduction/non-inclusion relating to transfers by UK permanent establishments (PEs));
- Chapter 8 (multinational payee deduction/non-inclusion mismatches); and
- Chapter 7 (hybrid payee deduction/ non-inclusion mismatches).

In addition, the amendments clarify the position in respect of timing mismatches and the interaction between the hybrid mismatch rules and the existing UK rules in relation to foreign PE losses, whilst also making a number of other technical amendments.

Where assessing the impact of the draft hybrid mismatch rules on any cross-border structure, careful consideration of these amendments will be required.

The key amendments are summarised below:

Chapters 6 (deduction/non-inclusion mismatches relating to transfers by PEs): The amendments limit the scope of Chapter 6 so that they only apply in relation to PEs where the UK is the payer jurisdiction. This ensures that the hybrid mismatch rules do not conflict with the UK foreign PE exemption rules.

Chapter 7 (hybrid payee deduction/ non-inclusion): The amendments extend the scope of the rules to arrangements where a payment is made to a hybrid payee which has no territory in which it is resident for the purpose of a tax charged, unless the hybrid payee is a CFC for UK or foreign CFC rules. This represents a significant departure from the final OECD Action 2 report (neutralising the effect of hybrid mismatch arrangements) as it means any mismatch where the payee is a hybrid entity (for example, a company treated as a disregarded company for US subpart F purposes) may potentially be within the scope of this rule, regardless of whether it arose by virtue of the payee being a hybrid entity.

Chapter 8 (multinational payee deduction/non-inclusion mismatches): The amendments limit the scope of Chapter 8 so that they only apply in relation to PEs where the UK is the payer jurisdiction. In addition, when determining whether the mismatch has arisen by virtue of the payee being a multinational company for the purposes of condition D of s 259HA(6), mismatches which arise because there is no corporate taxation in the PE jurisdiction are excluded.

Chapter 10 (dual territory double deduction cases): The amendments limit the scope of the dual territory double deduction rules, so that overseas permanent establishment excess deductions can be used in the UK unless those deductions have also been used overseas against the profits of another person where there is a multinational company and the UK is the parent. This ensures that the hybrid mismatch rules do not override the existing UK rules in relation to the availability of overseas PE losses. However, if the deduction is subsequently used overseas against