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The Return of Crown Preference

For many years, HMRC was entitled to a preferential claim in an insolvent matter in respect of arrears of PAYE, NIC and VAT and this position was more commonly referred to as Crown preference.

The Enterprise Act 2002 which came into force in September 2003, abolished Crown preference and relegated HMRC's claims into the unsecured creditor category. However, certain employee claims did retain their preferential status. The abolition favoured those parties holding floating charges who now received monies which previously would have been paid to HMRC.

In the **October 2018 budget**, the Chancellor announced that he would be **restoring some tax debts to preferential status** in corporate insolvencies which begin after 6 April 2020. The announcement came as somewhat of a surprise as there had been no consultation or prior indication of a change of policy.

The Government has now published a brief consultation document on its proposal but there is limited analysis of the impact on the return to unsecured creditors.

The proposal states that from April 2020, **tax debts** which a company 'owes on behalf of others' will become a **secondary preferential creditor in insolvency procedures**. This means that **PAYE, employees NIC, Construction Industry Scheme (CIS) and VAT debts move up in order of priority** to sit behind employees' preferential claims and deposits covered by the Financial Services Compensation Scheme but ahead of floating charge holders, unsecured creditors and shareholders. However, tax debts owed by the company itself such as employers NIC and Corporation tax will remain in the unsecured category.

At present, there is no time limit or cap on these new preferential claims. The intention is that whilst the proposal will only affect those insolvencies commencing after 6 April 2020, any tax due prior to this date will be treated as a secondary preferential debt.

The Government has indicated that the proposal will lead to an **additional £185 million being received by the Treasury every year**. It is claimed that the proposal will not have a material impact on lending or the return to unsecured creditors who, on average, only recover 4% of any debt owed. Any change which diminishes the return to a floating charge holder is bound to have an effect on lending policies whilst the 4% return to unsecured creditors looks likely to be reduced even further.

Please note that should your clients require any confidential advice regarding insolvency matters they are welcome to contact one of our partners. Initial advice is provided free of charge and without obligation. Also, if you or any of your colleagues require any clarification regarding insolvency law or procedures please do not hesitate to contact us.