

(UK) EBT Claims- Have Beneficiaries been Unjustly Enriched?

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Can a liquidator run an unjust enrichment claim to seek to recover PAYE and NIC liabilities from a company's directors arising from the company's use of a "disguised remuneration" employee benefit trust ("EBT") scheme? Based on the findings of ICC Judge Barber in the case of *Re Ethos Solutions Ltd*, the answer is "no".

EBTs: Background

The case is the latest in a series of cases arising from companies using disguised remuneration EBT schemes (such as the gold bullion schemes), with the company subsequently entering an insolvency process. These types of EBT schemes were designed to enable a company to make payments to its employees, usually its directors, whilst avoiding PAYE and NIC liabilities, and in some circumstances also aiming to provide corporation tax relief for the employer. The payments often took the form of loans from offshore trusts, that were never intended to be repaid.

HMRC challenged these schemes, as it claimed that their purpose was solely aimed at avoiding tax liabilities and comprised disguised remuneration that should give rise to the usual PAYE and NIC liabilities in respect of remuneration. The challenge was litigated all the way to the Supreme Court, who in 2017 held that the schemes did not work to effectively avoid those tax liabilities, and therefore that PAYE and NIC should have been paid on the sums paid to the directors under the EBT schemes.

The schemes have therefore resulted in claims being pursued by liquidators of insolvent companies against its directors, for causing the company to enter into the failed schemes and for the losses incurred by the company and HMRC as a result. As the schemes had often been used for a number of years prior to the company entering into insolvency, insolvency practitioners often had to rely upon claims that were not subject to the usual limitation/look-back periods, such as claims under s423 Insolvency Act 1986 (transactions defrauding creditors).

Case Summary

Ethos Solutions Ltd operated a disguised remuneration EBT scheme. Ethos entered into CVL in December 2012. HMRC submitted significant claims in the liquidation, relating to the unpaid PAYE

and NIC that was intended to be avoided by operation of the EBT scheme. In December 2018, Ethos' liquidator issued a claim against the various beneficiaries of the EBT scheme under s423 IA 1986, alleging that the payments to the relevant trust (and from there, to the directors) were transactions at an undervalue aimed at prejudicing HMRC.

In June 2022, the liquidator applied to amend the claim, to bring an additional and alternative head of claim based on unjust enrichment/restitution i.e. claiming that the respondents had benefited from the EBT scheme, at the expense of the company.

ICC Judge Barber refused the application to amend the claim, on the basis that the unjust enrichment claim had no reasonable prospect of success. In essence, the judge held that due to the operation of the various pieces of legislation that were introduced to combat disguised remuneration EBT schemes, the respondents already had a parallel obligation to account to HMRC for the relevant elements of the PAYE and NIC liabilities. Accordingly, unless the company had discharged those liabilities to HMRC (which would in turn have extinguished the respondent's parallel liability to HMRC), then the judge held that the respondents had not been enriched, as their liability to HMRC had not been extinguished.

On the basis that the purpose of the disguised remuneration EBT schemes was to avoid these tax liabilities and given that many companies that used such schemes are now in an insolvency process, it is highly unlikely that the relevant company would have paid those PAYE/NIC liabilities to HMRC. This case therefore makes it highly unlikely that liquidators will be able to run an unjust enrichment argument as an alternative to assist in recovering sums from beneficiaries of EBT schemes.

The case is also a helpful reminder of the need to fully plead a claim (and all alternative arguments) at the outset and avoid the need to seek to amend the claim if at all possible, particularly when the application to amend is made at a late stage. The burden will always be on the amending party to justify why it is appropriate to amend the claim at that stage. This creates a significant risk that permission to amend will be refused, as it was in this case, with the normal consequence being that a costs order is made against the party seeking to amend.

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