Check on powers

Mala Kapacee discusses the conclusions in the House of Lords' review of HMRC powers with some comparisons to HMRC's evaluation.

There are many interesting observations in the House of Lords' review of the new powers in Finance Bill 2021, though how much attention will be paid to it remains to be seen. Unless otherwise stated, all quotes are from the House of Lords Economic Affairs Committee, fourth report of session 2019-21 *New powers for HMRC: Fair and proportionate?* published on 19 December 2020 (tinyurl.com/holrepd20).

The review considered these measures introduced in Finance Bill 2021:

- tackling promoters of tax avoidance, including the related calls for evidence on raising standards in the tax advice market and disguised remuneration schemes;
- amendments to HMRC civil information powers; and
- new tax checks on licence renewal applications.

The report also covered a new requirement on large businesses to notify HMRC of an uncertain tax treatment, however this has been delayed until 2022 so we will not cover it in detail.

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Principled approach to powers

Every few years, HMRC undertakes a review of its powers. In 2007, it issued a consultation document *Modernising powers, deterrents and safeguards* from which it devised a series of

Key points

- Is HMRC taking on more powers than it needs?
- Promoters of mass marketed avoidance schemes must not be conflated with agents advising in the mainstream.
- House of Lords considered retrospective legislation for scheme promoters was acceptable.
- Changes to HMRC's civil information powers may deny taxpayers the tribunal safeguard.
- New tax check on licence renewal applications may go too far.

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principles which it undertook to adhere to when designing new policy. The House of Lords reviewed the most salient of these, namely:

- clear policy *objective*;
- *simplicity* in the definition;
- close *targeting* of the proposed policy;
- *proportionality* of the proposed power;
- ensuring *safeguards* are built into the policy to ensure the powers can only be used in appropriate circumstances and wielded in an appropriate manner; and
- proportionality of *sanctions*.

In 2018, the Lords recommended that the government recommits to the principles and that they should be formalised as an essential part of policy process. In response, the Treasury commissioned a review of the implementation of powers since 2012 (to 2018) but did not wait for the results of the review before preparing draft legislation in Finance Bill 2020. This suggests that whether the powers are implemented fairly, proportionally and consistently was not relevant to HMRC's request for new powers.

In short, HMRC has requested more powers before taking the time to understand whether the existing ones are adequate. It is clear to most tax investigations practitioners that HMRC already had a huge wealth of powers so new powers with reduced safeguards – for example, the new financial information notices – will only remove protection from taxpayers rather than adding quality to HMRC's already overflowing arsenal. The House of Lords' review correctly stated:

> 'Evaluating changes to HMRC powers enables review of their effectiveness, addresses unintended consequences, informs future policy developments and ensures the balance between HMRC powers and taxpayer rights is maintained.'

When questioned about the timing of proposals in the draft Finance Bill 2020, before the completion of HMRC's review,

the financial secretary to the Treasury responded: 'We are simply trying to improve our understanding of powers and safeguards as we go, and that work is already bearing fruit. We do not need to delay work that is already in progress in order to do that. In fact it would be wrong to delay things.' This further highlights that understanding existing powers and safeguards is secondary to gathering more powers.

The outcome of HMRC's own review – published in February 2021 – resulted in '21 commitments ... for a tax system fit for the 21st century' (tinyurl.com/hmrcevfeb21). Of these, six were to increase 'awareness' of processes and taxpayer obligations – but none of them talked about how this would be done – and five were about improving HMRC service and building trust – again without detail as to how they may wish to achieve this. Our view is that increasing powers without due consideration as to how existing powers are being used is equivalent to riding roughshod over taxpayer rights.

Why are we giving HMRC more powers when, according to the House of Lords it 'is still not making full and effective use of its existing powers, and should look to how these might be better used before considering new legislation'?

In summary, we agree with the Lords' conclusion that 'the government should have awaited the outcome of its own review into the operation of its powers and safeguards before further powers were proposed for HMRC. The outcome of its review should have been used to inform and frame the draft Finance Bill proposals. Evaluation of what has gone before must always be a useful means to determine the best way forward'.

Even better would be an independent third party to evaluate previous powers and look at whether new ones should be proposed. HMRC should clearly not be in charge of proposing its own powers.

Tackling promoters of mass marketed schemes

The House of Lords' review concludes that although on paper HMRC has committed to trying to penalise promoters of tax avoidance schemes, it is still in practice going after the 'low hanging fruit', namely taxpayers who were on the whole conned into using schemes that they were told were legitimate. The Lords ask 'whether HMRC has struck the right balance between focusing on individuals who used these schemes and the promoters of such schemes'. It would be interesting to see how HMRC responds to this.

By implementing retroactive taxation in the form of the loan charge, HMRC's target is clearly the users of the arrangements rather than the promoters or enablers. Further 'notwithstanding the various powers HMRC has accumulated in recent years, a number of promoters – the so-called "hard core" – remain in business, despite HMRC knowing who these promoters are'. This again indicates that HMRC has the knowledge and the power but is unwilling or unable, perhaps because of their limited resources, to go after promoters.

Many respondents suggested that the proposed sanctions against promoters were drafted so widely as to 'catch' normal tax advisers 'advising in the mainstream'. We compare these comments with the policy principles referred to above where HMRC committed to having 'targeted' policies. That said, EU Directive 2018/822 (DAC6) – albeit arising from an Organisation for Economic Co-operation and Development initiative – is also drafted incredibly widely and catches almost any piece of planning. Since leaving the EU, the relevant UK legislation has been significantly reduced.

HMRC's task now is to target the new measures narrowly at promoters to ensure that bona fide advisers are not caught, while also ensuring the promoters cannot argue they are out of scope. Given that the government recognises that promoters of mass market avoidance schemes are 'rarely members of a professional body' (HMRC policy paper *Tackling promoters of mass-marketed tax avoidance schemes,* see tinyurl.com/govtptasmar2020) perhaps targeting the unregulated advisers first would be a good start. Further, to help the public, the term 'tax adviser' could be protected so those who use it without suitable professional qualifications are prevented from doing so.

The House of Lords also considered whether retrospective legislation in relation to promoters of schemes was appropriate. It found: 'HMRC must apply symmetry to taxpayers and promoters; neither should be pursued for actions before HMRC found they were illegitimate, but both should be held accountable for their actions after that point.' Does that mean that promoters of disguised remuneration schemes after December 2010 will be prosecuted? Let's wait and see.

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Civil information powers

Details of HMRC's civil information powers are in FA 2008, Sch 36. These cover requests for information from the taxpayer and also from third parties. Currently, to request information from third parties, HMRC needs either taxpayer or tribunal approval. The proposed amendment to these powers would result in HMRC no longer having to seek such approval to issue a third-party notice. In most cases, it would simply have to advise the taxpayer the information had been requested.

Bearing in mind the principles of policy making listed earlier (specifically safeguards), an obvious point comes to mind – if HMRC no longer needs taxpayer or tribunal approval, what is to stop it going on 'fishing expeditions'? The Sch 36 legislation is already broadly drafted requiring only a 'reasonable suspicion' of an underpayment of tax for information to have to be provided. Most would consider these powers sufficient.

HMRC's case for removing the approval process is that an Organisation for Economic Co-operation and Development report, *Global forum on transparency and exchange of information for tax purposes* (tinyurl.com/oecdglrep), claimed that the UK's processes 'unduly delayed the effective exchange of information'. HMRC considers this is due to the time taken to obtain approval.

However, the draft legislation also allows HMRC to request information in relation to the direct collection of tax debts

and only allows the third party right of appeal against penalties, rather than if the request is too onerous. Clearly, this proposal goes much further than speeding up the process for overseas tax authorities requesting information.

In 2018, when these measures were proposed, the House of Lords rightly said 'Oversight by the tax tribunal of HMRC attempts to obtain information from third parties is an important taxpayer safeguard, which should not be removed without good reason. HMRC has not offered a convincing rationale.'

> "This does then raise the question, if the process is so efficient, why did the OECD consider it a problem?"

Two years down the line, draft legislation on the proposal was published after a brief consultation which overwhelmingly showed respondents concern about the withdrawal of taxpayer rights, with some saying that HMRC's powers were already adequate (tinyurl.com/hmrccondocahcip). Again we refer to HMRC's review of its powers and its commitment to increasing trust between taxpayers and HMRC. We are unsure as to how implementing proposals that remove taxpayer safeguards help here, in particular when consultation responses advised against it.

If opinions that are actively sought by HMRC are actively ignored we question the value of the process. Having seen requests made under Sch 36 for information that is neither reasonable nor relevant to a taxpayer's tax position, it is clear why so many respondents were concerned about this proposal.

Any suggestions proposed to streamline the process to minimise delays were dismissed by HMRC; one of the responses was that 'HMRC and the Ministry of Justice had already made the process as efficient as possible'. This does then raise the question, if the process is so efficient, why did the OECD consider it a problem? That said, Covid-19 has resulted in many tribunal processes being streamlined so it is hoped this should solve the matter HMRC ostensibly wanted addressed.

The House of Lords also reviewed the number of requests that were sent to tribunal and concluded: 'It is disproportionate to deny UK taxpayers the tribunal safeguard for the sake of speeding up a small minority of cases involving international requests.'

Even more telling about HMRC's attitude and the reasons for wanting to introduce financial institution notices is its comment: 'When we looked at the timeline for obtaining the information, the step of getting the additional information required from the other tax jurisdiction was taking over eight months on average. Even on its own, that step means that it is not possible for the UK to meet the international standards.' On this basis, it is unclear how adding to HMRC's powers will help to achieve its goal of reducing the time taken to respond to information requests from overseas. One could be forgiven for thinking that perhaps there is an ulterior motive.

The House of Lords roundly criticised this measure in respect of the policy principles as 'poorly targeted,

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disproportionate in their effect on UK taxpayers and lacking necessary safeguards and rights of appeal'. It suggested several changes to the legislation to reinstate the safeguards and reconsider the date of implementation. It remains to be seen whether the House of Lords holds any more sway than the various professional bodies and other stakeholders.

Notifying uncertain tax treatment

In essence, this measure requires companies undertaking a transaction based on an interpretation of legislation that may differ from HMRC's, to tell HMRC of the 'uncertain tax treatment'. The consultation was issued at stage 2 of the policy, meaning that HMRC had already committed to it and was looking at how best to implement it, rather than outlining the issue and looking for suggestions on how to deal with it (stage 1).

The responses to the consultation suggested that, as large businesses already have HMRC customer compliance managers, the department is already likely to be aware of any potential issues. Adding an additional burden to these taxpayers would be unhelpful and unlikely to result in significant gain to HMRC in closing the tax gap due to different interpretations of tax legislation.

The House of Lords advised HMRC to start at the beginning with a stage 1 consultation to work out whether such a measure was necessary in the first place.

Licence renewal application

Here, HMRC proposes that when an individual wishes to renew a licence to drive a taxi or minicab, they would have to undergo a tax check before the licensing authority considers the application for renewal.

To its credit, HMRC has consulted on the proposals twice and appears to have taken account of the responses, noting that most respondents seemed to be in favour of the proposal and changed the affected sectors in response to the second consultation. There were questions on whether this measure would assist in increasing compliance or whether people would find ways to avoid the check or potentially just continue to drive without renewing their licences. If HMRC pushes people too far, does it drive non-compliance further underground?

Others also commented that the consultation suggested the condition for a renewed licence would concern whether a person was registered for tax whereas the draft legislation required more information would have to be provided before the condition is satisfied. On this point, the House of Lords said: 'Once there has been a consultation, major changes to proposals should not be made without explanation.'

The report noted also that there is no explanation of how particular sectors have been targeted and requests for more information appear to have resulted in only vague indications 'the decision to proceed with the two sectors … was based on a wider range of criteria'. The House of Lords requested a detailed analysis of why the specific sectors were chosen before the measure goes ahead but it was implemented in Budget 2021 with no further public discussion (see tinyurl.com/hmrclicencechs) and the legislation is currently making its way through parliament.

Planning point

Make sure that taxi drivers or scrap dealer clients who have to renew their licence are aware of the new requirement to satisfy a tax check.

To my mind, there is another danger here. Once this legislation is brought into force for sectors which require government authorisation, it will be easy to adjust it to cover public sector workers and then another small step for employers to have to request future employees to obtain a certificate of tax compliance from HMRC. It might seem far-fetched now, but, as we saw with the IR35 changes, it is most definitely possible.

In Estonia for example, as all records are digital, anyone can request access to view areas of someone's tax records before agreeing to do business. It may not be a condition of doing business but sharing the data may become so mainstream that not sharing could have a negative impact on the individual or business. In the UK, tax affairs are confidential and salaries are not discussed as widely as in some other countries. There are arguments for and against privacy in relation to tax and this is a discussion that needs to be held.

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Independent oversight?

There are a lot of concerns about powers which give HMRC the right to use its 'discretion'. Given the department's intention to exercise powers consistently and to build trust between itself and the taxpaying public, oversight of HMRC by an independent body would be welcome.

Despite the criticism, Budget 2021 confirmed that the amendments to the civil information powers and the tax conditionality for licensing would be brought into force. This begs the question – what value does HMRC place on external consultations and on parliamentary opinion? Is it time for independent oversight of our tax policy writers?

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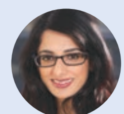

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