



Taxing Matters

What “winning on a technicality” really means in HMRC disputes with Harry Smith

Alice	<p>Hello, and welcome to Taxing Matters, your one stop audio shop for all things tax brought to you by RPC. My name is Alice Kemp and I will be your guide as we explore the sometimes hostile and ever-changing landscape that is the world of tax law and tax disputes. Taxing Matters brings you a fortnightly roadmap to guide you and your business through this labyrinth. In case any of you miss any crucial information or just want some bedtime reading, there is a full transcript of this and indeed every episode of Taxing Matters on our website at www.rpc.co.uk/taxingmatters.</p> <p>Today we will be talking with Taxing Matters favourite, Harry Smith. Regular listeners will remember Harry from our episode where he explained the duties and obligations on HMRC as a result of being a public authority. Well, Harry is back today to give us another crash course in how procedural arguments, sometimes referred to unfairly as "technicalities", operate in the context of a dispute with HMRC.</p> <p>Harry, welcome to Taxing Matters.</p>
Harry	<p>Thank you, Alice, it's good to be back.</p>
Alice	<p>Well, we hear, sometimes, people talking about winning a dispute on a “technicality” or a “procedural” point. What does this mean in the context of a dispute with HMRC?</p>
Harry	<p>Well, I suppose it's quite useful if we step back and just consider for a moment why we have these technicalities, these formal requirements.</p> <p>If you're, for example, an individual or a company and you're filing a tax return, of course you expect that there's going to be a deadline. This is to enable the Revenue actually to assess the tax; to mean that people don't constantly delay in letting the Revenue know what their self-assessment is.</p> <p>And, really the same cuts both ways. Just as an individual has to file their tax return the company has to file their tax return by a deadline - you know, a certain number of months, certain a number of days depending on what it is, after a taxable event or after the end of a tax period.</p> <p>So too the Revenue has got some procedural requirements that it needs to abide with. And the reason for this is just to ensure that everything runs smoothly and to ensure that people know where they stand.</p> <p>In an ideal world, just as the Revenue want to know what people have done that is taxable, so too individuals and companies have the right to expect that after a certain amount of time their tax affairs for a certain period are going to be final.</p> <p>So HMRC has a set period of time in which to open an enquiry and, that period of time depends on the specific facts, but ultimately it is due to certainty and to enable tax systems to run efficiently.</p> <p>So when we talk about winning on a technicality it's not so much, you know, a cheap point. And I agree that there was the perception certainly a few years ago, particularly among big four accounting firms actually, that procedural points weren't, weren't fair game really that they were sort of the last refuge of the scoundrel. And if all you were doing was relying on a procedural point, then you didn't really have a proper case.</p> <p>The procedural points are there for a reason and they are there, you know, on one side to protect the Revenue and on the other side to protect the taxpayer as well. So, there shouldn't be any sort of stigma attached to winning on a procedural point.</p>
Alice	<p>So, you've just talked there about opening an enquiry, what do you mean by opening an enquiry and why is that important?</p>
Harry	<p>An enquiry is HRMC's process for looking into, to state the obvious, a tax return, you know, it does what it says on the tin after all.</p> <p>And the time period in which they can do that varies, so they can open an enquiry - just looking at the world of direct tax - within 12 months of a return going in.</p>

If they discover something, and I think we'll come back to discovery assessments later on, if they discover something that they didn't know before but that they kind of should have known, then that can give them grounds to open an enquiry. If they discover a loss of tax due to a mistake, they can open an enquiry within four years; within six years if the error is careless; and within 20 years if they think that error is deliberate - so if someone's, you know, blatantly lied on their tax return and said “no, I didn't earn any money this year”, when actually they took home a couple of million.

So, that is what opening an enquiry is, and the consequences of this are that it kicks off some rights and some obligations, both for the Revenue and for the taxpayer. So, again we have this two-sided coin: HMRC can ask for certain information using information gathering powers that are set out in the relevant legislation, so just sticking with direct tax within in the Taxes Management Act. And individuals too have got the right to ask for this enquiry to be brought to a close; so they can apply to the First Tier Tribunal for a closure notice (which is the document that the Revenue issue when they finished their enquiry).

And again, this is to help certainty; so that you don't have enquiries dragging out for years and years and years and the taxpayers not knowing where they stand.

Alice **So what are the requirements before an enquiry can be opened?**

Harry Well, I mean, as I said initially, so if they get on it quickly, then, really, they can open an enquiry just if they think “we better look into this”. And in the past HMRC have carried out campaigns targeting specific groups of taxpayers - I think one of their initial sector-based campaigns was based on dentists, I'm not sure why that sticks with me, but I suppose it's more memorable than some other groups - don't ask me when I last had a check-up.

Or they could have some sort of intelligence that a return might be inaccurate, so they gather information from all sorts of sources; from banks providing information as they are obliged to do under some of their reporting requirements. And foreign jurisdictions; they may have received information under the Common Reporting Standard or some other automatic exchange of information or pursuant to an information request.

And there are plenty of reasons that give HMRC valid grounds to open an enquiry and, as I say, they can do so within certain time limits depending on what is in the return, depending on what they think the insufficiency is.

Alice **So how can one tell if an enquiry has been opened and they have got these information gathering powers and other obligations arise, or if it hasn't?**

Harry Well they have to let you know. Which is an absolute key as in order for an enquiry to be opened validly, HMRC have to send a notice of enquiry and they have to send that notice of enquiry to the right taxpayer.

In the case of an individual this is, this sounds pretty facile, they can't send it to your next-door neighbour. But in the case of groups of companies for instance, this is very important, because they've got to get the right corporate entity or the right member of a group and if they get that wrong then the enquiry can be invalid, with all the consequences that flow from that.

So, there's a really important illustration of the importance of getting a notice of enquiry right for the Revenue. And this is a case involving a company in the Credit Suisse Group . In that case the tribunal found that a valid notice of enquiry hadn't been issued.

What had happened is that there had been a continuum of correspondence where HMRC hadn't quite got to the enquiry stage yet, but they were sniffing around the bank's payroll tax return. And they had had a lot of informal correspondence - just by email - with people in the tax department and part way through the process the person handling the investigation at HMRC changed. And they got all the way to issuing a closure notice - by which time they would have been out of time to open an enquiry - and the taxpayer turned around and said “woah, woah, woah, there isn't actually a valid enquiry here”.

And the Tribunal agreed.

They hadn't notified the taxpayer with enough specificity for them to be sure that there was an enquiry. And it was a perfectly reasonable view, to a reasonable person in the shoes of the tax manager, but actually HMRC were just carrying on with their informal non-enquiry enquiries, to use a horrible phrase.

So, the assessments that were issued, well, purportedly issued, in the closure notice and the amendments to the return were held to be invalid. And this is particularly striking because the Tribunal, just in case they were wrong on that point, then went on to consider whether or not, on the substance, the Revenue would have won. And they held that they would have done.

So, it is clearly only this procedural point that has saved the taxpayer's proverbial bacon.

	<p>And, it's very striking - it's a prominent taxpayer, a lot of money at stake - bank payroll tax doesn't tend to come cheap - and you know, if you were the Revenue officer involved, you'd feel quite embarrassed. And I think there was just a breakdown of communication, the new person handling the enquiry, handling the non-enquiry I suppose, the new person handling the affairs of the corporate just assumed that the enquiry was in place and so didn't actually go back and check.</p>
Alice	<p>What about the scope of the enquiry itself? Once an enquiry is open, is it a free-for-all or are there limits on it?</p>
Harry	<p>It's more of a free-for-all than you might expect.</p> <p>So, it is into everything that is contained in a return. So, you know, looking at individual taxpayer you've got, your employment pages, you've got your capital gains pages, your income and property pages, and all of that can technically fall within an enquiry.</p> <p>What it can't do is to go into something that isn't in that return or isn't in the thing that is being enquired into. So, you know, they can't go off and look at your VAT, because that's separate.</p>
Alice	<p>But other than that it's pretty much anything that you've said in that particular return can be enquired into?</p>
Harry	<p>Yes, that's right.</p>
Alice	<p>So you mentioned earlier discovery, what is discovery?</p>
Harry	<p>So a discovery is, again, it's sort of what it says on the tin, it's something that HMRC find out that they didn't know before, that affects the position for this particular taxpayer, this particular return or claim.</p> <p>It could be something that the taxpayer omitted to mention in a return. That's the sort of classic example.</p> <p>To reduce it to a really simple example, if a taxpayer doesn't mention on a tax return that he's sold a property and then the Revenue find this out, then that would be grounds for the Revenue opening an enquiry because they have discovered something.</p>
Alice	<p>So how do the time limits and other details, differ from opening an enquiry under normal circumstances.</p>
Harry	<p>So, in some respects it's the same process, you know; the Revenue still have to send a notice of enquiry, it's just that they have longer in which to do it.</p> <p>If they discover a mistake leading to an insufficiency of tax then they have four years from the date on which the return had to go in; if that mistake is careless then they have six; and if it's deliberate then they have 20.</p>
Alice	<p>So what kind of facts might lead to a discovery assessment?</p>
Harry	<p>Well you may or may not be surprised to know, there has been some recent caselaw on this, and, it's quite interesting because this particular case is a case of Tooth - so linking back to my example about dentists earlier, in name only I'll admit.</p> <p>This particular case has gone all the way up to the Court of Appeal and each level of court has decided it on slightly different grounds.</p> <p>So, this was a taxpayer who had done a scheme, which was intended to create some employment losses and his accountants were using some software that was approved by HRMC which didn't allow these losses to be entered on the right pages; the employment pages wouldn't let them put a negative number in, so what they did instead is they put, they'd just put zero in there and then made a disclosure in the white space, sort of the "notes" bit of the tax return, "this is what we've done here, this is a loss". And HMRC challenged this, but they only challenged it quite late in the day, so their ability to challenge was dependent on them having "discovered" something.</p> <p>The First Tier, they held that the Revenue had made a discovery because they had looked at the return and actually some other facts had come to light but the conduct that was complained of wasn't deliberate (because they were so far, you know, behind the curve, that they had to show that there had been some deliberate conduct - so they were within that six to twenty year period).</p> <p>And the First Tier held that this wasn't deliberate; the taxpayer and his accountants had been completely above board, nothing to see here.</p> <p>The Upper Tribunal discarded it on slightly different grounds, they held that again, that there wasn't a deliberate error, but actually there wasn't an inaccuracy because although the wrong numbers had been put in the employment pages, they had been corrected elsewhere in the return.</p>

The Upper Tribunal also made an interesting observation, although they didn't need this to get to the result they reached, they thought that the discovery had gone "stale"; the Revenue "discovered" it in 2009, but they didn't issue an assessment until 2014, and so they brought in this concept that the Revenue have to act with a reasonable degree of expedition when they find something out.

The Court of Appeal went a bit further, they said actually it's not enough, in terms of making a discovery assessment, it's not enough for the Revenue just to have discovered a new reason that the wrong amount of tax is stated, they have to actually discover the insufficiency itself.

And this was a split Court of Appeal; they were split about whether or not there was an inaccuracy, two thirds of the court thought that actually there was an inaccuracy, even if it was corrected elsewhere in the return, but they did all agree that, if there was an inaccuracy, then it would have been deliberate, so, slight splitting hairs here.

But really the key concept is that the Revenue have to make a substantive discovery, they can't just find a new reason for "oh, and another thing, this is wrong because..." they have to actually find out about the insufficiency itself.

Alice **So you've mentioned this in the context of tax, does this also apply to customs or other obligations that taxpayers have to HMRC?**

Harry we're not just in the world of direct tax; there are procedural obligations throughout the tax code construed very broadly.

There was a case came out fairly recently about a man who had, I mean it's hard not to feel a great deal of sympathy for him when you read the judgment of the Tribunal: the case of Mosson.

He had been to Belgium to buy some rolling tobacco for his wife and he did the same six months earlier and he was planning to do the same in another six months. And he was in poor health and he had an interview with a customs officer, which he had to leave after the better part of an hour because he wasn't feeling very well.

And at the end of this interview, the customs officer took 5 minutes and seized the tobacco on the basis that it wasn't genuinely for his wife, it was being imported for commercial use, he was planning to sell it.

But he hadn't taken the taxpayer's address and, you know, the taxpayer wasn't there to be given the notice of seizure.

So, despite the fact that the taxpayer didn't appeal a notice of seizure in time, the Tribunal held that well, of course he hadn't, because he hadn't been given it and so the Tribunal remade the customs officer's decision.

And you can almost see them shaking their heads through the words that they had written down and, yeah, I suspect that it was very convenient for them that there was this procedural foot fault by the Revenue to enable them to give this man his tobacco back and vacate his penalties.

Alice **So probably the right decision arrived at on those facts.**

Harry Yes. On the facts, actually the customs officer hadn't asked how much the man's wife smoked and how quickly she was going to get through this tobacco, so, it was a fairly deficient process all round.

But it just goes back to the point that procedural requirements are in place for a reason. They're there to protect the Revenue and they're there to protect taxpayers as well.

Alice **So, what advice would you give to any business who is faced with an enquiry or a discovery assessment and is thinking "what do I need to look at first"?**

Harry I think key is the notice of enquiry.

And, depending on what stage you've got to in your enquiry, you know, the enquiry may have finished and there may be a closing notice and if there is, it's always tempting just to look at that.

But it is always worth just looking back and checking off in your head; has an enquiry been validly opened? Is it addressed to the right taxpayer? Is it addressing the correct periods, you know, the right tax return?

There are a lot of things that, it's very easy to miss and, you know, 99 times out of 100, everything will be in order, but on the one time that it isn't, it is dropping the ball a bit just to think “oh, well, let's just go on and litigate this” when there may be a very easy and practical way of saying “woah, woah, woah, hold on guys, we don't think there has been a valid enquiry, we don't think that these, assessments that have been issued at end of this enquiry are valid”.

And that can save a lot of time in substantive litigation, it can save a lot of time and a lot of money in legal fees as well. Not wishing to do myself out of a job but.

Alice **Those points can be useful.**

Harry Those points can be very useful.

Alice Well thank you very much Harry for taking us through how procedural points operate to protect taxpayers in the context of a dispute with HMRC.

As ever a big thank you goes to our miracle working producer Mary Mitchell; Josh McDonald, who does all the work pulling each episode together; our music is from musical genius Andrew Waterson; and of course a big thank you to all of our listeners for joining us.

A full transcript of this episode, together with our references can be found on our website www.rpc.co.uk/taxingmatters.

If you have any questions for me or for Harry or any topic you would like us to cover in a future episode please do email us on taxingmatters@rpc.co.uk; we would love to hear from you.

If you like Taxing Matters, why not try RPC's other podcast offering, Insurance Covered, which looks at the inner workings of the insurance industry hosted by the brilliant Peter Mansfield and available on Apple Podcasts, Spotify, Acast or our website.

If you liked this episode please do take a moment to rate, review and subscribe and remember to tell a colleague about us.

Thank you all for listening and talk to you again in two weeks.



RPC is a modern, progressive and commercially focused City law firm. We have 97 partners and over 700 employees based in London, Hong Kong, Singapore and Bristol. We put our clients and our people at the heart of what we do.