

Tax Enquiries: Closure Rules
Response from the Low Incomes Tax Reform Group (LITRG)

1 Executive Summary

- 1.1 We agree that the current closure rules on tax enquiries need to be revisited and updated as tax legislation has become more complicated since the introduction of the self assessment rules.
- 1.2 However, we consider the proposals to be one-sided favouring HM Revenue & Customs (HMRC), potentially enabling HMRC to choose specific areas of an open enquiry to take to Tribunal whereas the taxpayer has no similar rights or powers. We would prefer to see a more balanced approach where both parties have the power to refer to the Tribunal to seek partial closure of certain aspects.
- 1.3 There are insufficient safeguards to protect vulnerable groups and low-income taxpayers, we recommend that a *de minimis* limit on the potential tax at stake is used and that the usage of 'sole referral' and 'Tribunal Referral Closure Notices' are monitored.

2 About Us

- 2.1 The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.

- 2.2 LITRG works extensively with HM Revenue & Customs (HMRC) and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.
- 2.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

3 Introduction

- 3.1 We welcome this opportunity to respond to the Stage 1 consultation on the proposed amendments to the closure rules for tax enquiries. As LITRG primarily focuses on income tax and National Insurance contributions (NIC), we will address comments on this response with respect to income tax and NIC enquiries only.
- 3.2 LITRG is an initiative of the CIOT; we support the CIOT's separate submission. Our response focuses on points of concern that have direct relevance to the low-income taxpayer. We appreciate that the intention is that the new power should be used sparingly, in cases involving significant tax under consideration or involving issues that are novel, complex or have a wider impact. While it is unlikely that cases involving low-income taxpayers will have significant tax at stake, it is not uncommon for issues that are novel, complex or have a wider impact to arise in such cases. Hence our wish to see more robust safeguards than a vague policy intention set out in a consultation paper.

4 Question 1. We would welcome views on the problem as expressed in this document.

- 4.1 We understand that where there is an enquiry by HMRC into complex tax affairs it can be a long and frustrating process for both the taxpayer and HMRC. This is due to the current rules preventing the formal resolution of one issue without finalising and closing the whole enquiry; the exceptions to this being if both the taxpayer and HMRC refer a specific issue to the Tribunal or enter into a contract settlement. There are occasions, however, whereby a delay in the closing of a tax enquiry may be due to HMRC and not the taxpayer; this does not seem to be recognised in the consultation.

We also appreciate that where there is a significant amount of tax at stake that HMRC will want to receive payment relating to resolved areas of a still 'open' enquiry. We understand that this can be a problem when the taxpayer refuses to make a payment on account in relation to the disputed amount of tax. However, the Accelerated Payment regime should have removed this issue in cases of avoidance schemes notifiable under DOTAS and the

GAAR and, additionally, HMRC have the power to use jeopardy arrangements if there is a risk that the taxpayer may leave the UK.

5 Question 2. Do you agree to the proposed changes to the tax enquiry process?

- 5.1 We understand that HMRC have proposed these amendments to the existing rules in order to attempt to close tax enquiries which are taking a significant length of time to proceed or where there is potentially a large amount of tax at stake. While we acknowledge that the introduction of the proposed new rules could potentially provide greater certainty for both HMRC and the taxpayer we have a number of concerns with the proposals, which are stated in detail below.
- 5.2 The consultation contains examples at Annex C of the types of enquiries upon which the proposed changes would be used that include a taxpayer using several tax avoidance schemes. However, we have serious concerns that if these proposals are adopted without appropriate safeguards then low-income tax payers may be affected by these new rules contrary to HMRC's original intentions. For example, the use of these rules only in cases of high net worth individuals or large businesses may over time be relaxed due to a change in policy or general acceptance in the use of any long running enquiry and therefore low-income taxpayers may then be affected by these new powers.
- 5.3 We recommend that a *de minimis* limit for the potential 'tax at stake' should be used. This would act as a safeguard so that these new powers are only used exceptionally in complex and long running enquiries where there is a significant amount of tax at stake.
- 5.4 The proposed powers appear to be completely one-sided with HMRC able to be a 'sole referrer' to the Tribunal but not the taxpayer. We have concerns that these proposals may be against the spirit of the Taxpayers' Charter as they could not be described as 'even-handed'. We would welcome amendments which are less one-sided such as enabling taxpayers to be able to also consider 'sole referral' to the Tribunal if specific conditions are met. We understand that the CIOT and the Association of Taxation Technicians are also supportive of having a process whereby either the taxpayer or HMRC could be a 'sole referrer' to the Tribunal, which would result in a fair and balanced approach to both parties. There is a risk that if only HMRC can make a 'sole referral' to the Tribunal that certain open aspects of an enquiry will be cherry-picked by HMRC and resolved quickly while other aspects could be left on the backburner. For example, HMRC may refer aspects of an enquiry that are likely to be decided in their favour but not aspects which they expect to be found in the taxpayer's favour. This issue could be resolved by allowing both parties to refer aspects to the Tribunal and to partially close aspects of the enquiry.
- 5.5 The consultation does not discuss whether these amendments would be retrospective or be enacted on new enquiries. We would welcome clarification on this and further consultation if it is proposed to be acted on any enquiries which are currently open.

6 Question 3. Do you have any suggestions concerning the terminology of the new notice?

- 6.1 As explained at 5.4 we would welcome the opportunity for the taxpayer to also be a 'sole referrer' if specific conditions were met. For example, in the case of a multi-aspect enquiry where there is a specific matter such as quantifying a tax loss and the taxpayer had provided all relevant information to HMRC and was keen for closure on this particular matter then the taxpayer should also be able to make a 'sole referral' to the Tribunal.
- 6.2 We would expect that any new procedures introduced including new terminology to be clearly explained so that unrepresented taxpayers can understand any changes to the enquiry process. It is important that this information is provided in a variety of formats and not just online.

7 Question 4. Do you have any suggestions for how the proposed changes might be adapted to those limited cases where the tax treatment of a particular issue is no longer in dispute?

- 7.1 We understand that in cases where the tax treatment of a particular issue is no longer in dispute but there are other aspects under enquiry that HMRC would want that specific matter closed and any tax due paid (if it has not been settled through payment on account or contractual settlement). However, the application to the Tribunal by HMRC could be an expensive and formal approach to close a specific issue. We instead recommend considering using the Alternative Dispute Mechanism or the contractual settlement procedures as these methods may be more time efficient and less costly.
- 7.2 In cases where the tax treatment of a particular issue is no longer in dispute and it is in favour of the taxpayer, we would welcome an amendment to the proposals for the taxpayer to be able to 'close' that aspect and be able to utilise the tax advantage.
- 7.3 We would anticipate that where there is a Tribunal ruling then HMRC only applies the ruling to other open cases where the facts are **exactly** the same. If this is not the case and HMRC uses the ruling in cases with similar but not identical facts then there would need to be a further Tribunal hearing to decide whether the cases could be joined or not.

8 Question 5. Do you agree with the proposed amendment to the joint referral process?

- 8.1 The issuing of a 'Tribunal referral closing notice' must only be processed after the time has passed for the taxpayer to appeal against the First Tier Tribunal's decision. There must be safeguards in place to ensure all proper procedures are adhered to and that the taxpayer fully understands the appeal process as it is proposed that there can be no right of appeal against the 'Tribunal referral closure notice'.

9 Question 6. Should any other taxes be included in the scope of the proposal?

- 9.1 We do not consider that any other taxes should be included, however, the consultation does not mention how these proposals would interact with tax credits, given that the Tax Credits Act 2002 specifically relates the time limit for tax credit enquiries to the closure of the tax enquiry in some cases. Have the implications for tax credits and the tax credit compliance processes been considered?
- 9.2 Although the consultation states that HMRC will 'target the powers narrowly at cases or issues involving significant tax under consideration or involving issues which are novel, complex or have a wider impact'; we refer to paragraph 5.3 above regarding the need to have a *de minimis* limit to protect vulnerable taxpayers.

10 Question 7. Do you agree with the proposed governance safeguards?

- 10.1 Although these proposals are to be used 'sparingly' in cases where there is significant tax at stake we consider that safeguards are vital to protect vulnerable groups and low-income taxpayers. Throughout the consultation document there are numerous references to the proposed new powers only being used in cases of tax avoidance and where there is significant tax at stake or where there are complex tax issues which could have a wider impact. However, the only proposed safeguard is the use of independent HMRC staff to use their judgement over which enquiries should fall under these new powers. We do not think this safeguard is sufficient and would recommend that additional safeguards are used and these are detailed in our response to question 8 below.
- 10.2 It is important that HMRC adhere to their proposed safeguard of using 'nominated senior officials', who are independent of the open tax enquires, to approve of 'sole referrals' to the Tribunal and use of 'Tribunal referral closure notices'. It would be unfortunate if in the future due to financial constraints this safeguard was undermined due to pressure on HMRC's resources.

11 Question 8. We would welcome views on any additional safeguards to constrain the use of this proposal.

- 11.1 We strongly feel that there are insufficient safeguards in place to protect taxpayers especially when the powers are so one-sided to HMRC's benefit. We would expect the following safeguards to be included:
- 11.1.1 There should be a *de minimis* limit on the anticipated 'tax at stake' so that vulnerable and low-income tax payers do not get embroiled within these new rules when it is not designed to be targeted towards them. This would also protect low-income tax payers in the future from any scope-creep after these amended enquiry rules are established and their original purpose may be unintentionally forgotten.

- 11.1.2 It is important that these subjective HMRC powers are not included in any management targets. For example, there must not be a target for the number of 'Tribunal Referral Closure notices' issued. Each enquiry must be considered independently and the new powers only used where appropriate.
- 11.1.3 We recommend that information relating to these new powers such as the numbers of 'sole referrals' and 'Tribunal Referral Closure notices' issued and the reasons for doing so are published and are reviewed internally by HMRC so they can monitor and ensure that these powers are only being used where appropriate. For example, information such as the number of Tribunal referrals applied for, numbers proceeded with, numbers granted by the Tribunal, and the highest and lowest amounts of tax at stake could be reported on annually in the Tax Assurance Commissioner's Report.
- 11.1.4 If these proposals are to be used on current open enquiries then consideration must be given to how taxpayers will be made aware of these changes and what assistance they will need to understand the new rules.

12 Question 9. Do you agree with the assessment of impacts?

- 12.1 We consider that further work needs to be done to fully consider the impact on the Tribunal service by making these amendments. This research should be carried out as soon as possible to confirm whether these proposals would be economically viable because if the Tribunal service is unable to cope with these extra cases then these new powers will not speed up the tax enquiry process.
- 12.2 There will also be an increase of costs to both the taxpayer and the Tribunal service by potentially visiting the Tribunal on several occasions for a single tax return enquiry. Again, we make the point that there need to be safeguards in place to protect the unrepresented low-income taxpayer, who cannot afford the time spent nor costs involved in going to the Tribunal and may not understand the relevant processes which consequently may restrict their opportunity to successfully argue their case against HMRC.
- 12.3 As stated above at 11.1.3 we would recommend that the use of the 'Tribunal referral closure notices' are monitored so that it can be confirmed that the impact is only 'on those individuals on above average incomes with complex tax issues and those who engage in tax avoidance' and not on lower income and vulnerable groups of taxpayers.