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# Collaboration is key

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**M**uch media attention on tax evasion and avoidance is focused on multinational corporations or the rich and famous, but HMRC is increasingly targeting non-compliance by more ordinary businesses and their owners which accounts for a significant proportion of the tax gap.

HMRC's wealthy and mid-sized business compliance directorate (WMSBC) is responsible for monitoring compliance of more than 100,000 businesses with turnover between £10m and £200m. During 2015 HMRC's high net worth unit, which deals with individuals whose wealth exceeds £10m, was incorporated into the WMSBC.

The WMSBC has an established programme of 'cross-tax enquiries' for businesses that HMRC determines are at high risk of non-compliance. Businesses are selected for a review of their compliance with all tax regimes, and may include the financial affairs of the directors.

The way cross-tax enquiries are conducted by WMSBC can seem quite different from the way HMRC deals with large business enquiries. In one sense this is understandable because large businesses have a continuing dialogue with HMRC, so it should not be a surprise when, after an initial risk assessment, a particular issue becomes the subject of formal enquiry. By contrast, a WMSBC cross-tax enquiry will come as a surprise or, more likely in the eyes of the business, a nasty shock. Nevertheless whatever the 'type' of enquiry, it should be worked by adopting a collaborative approach in accordance with HMRC's litigation and settlement strategy.

A mid-size business might question what working collaboratively with HMRC means in practice.

Being collaborative does not mean doing whatever HMRC might propose in an enquiry. The business will possess knowledge and evidence of how it manages tax and be well placed to propose to HMRC how to address any potential risks

identified. Collaborative working entails a bilateral approach and could therefore be described as having joint ownership of the process.

## Opening letter to business

The opening enquiry letter will confirm that the business has been selected for a review that will cover the whole of the business and its operations. Some opening letters confirm that the directors' tax affairs will also be subject to review from the outset. But other enquiries might subsequently extend into these affairs if there is a blurring between company and personal arrangements.

HMRC will have conducted some risk profiling in selecting the business, but the reasons for the enquiry will not be stated. The letter will confirm that HMRC would like an initial meeting with the business and its advisers to discuss the operations of the organisation, the record-keeping systems, and the accountancy and audit input.

Some opening letters have included a list of business records – link papers between accounts and tax returns – that HMRC will expect to remove and review after the meeting. A request may also be made for computerised records. These usually cover a year for corporation tax, two years for employment tax and four for VAT.

The opening letter will be accompanied by a notice (FA 1998, Sch 18 para 24) opening an enquiry to protect HMRC's position together with a factsheet confirming the company's rights and obligations.

## Initial meeting

Although at this point the business will be in the dark as to why HMRC has opened an enquiry, much work can be done before the initial meeting. It will be an opportunity for the business to:

- confirm to HMRC how compliance with the various taxes is managed generally;

### KEY POINTS

- HMRC's WMSBC monitors businesses with turnover between £10m and £200m.
- Opening letters do not include the reason for the enquiry.
- Asking HMRC to be transparent about perceived risks may speed up the enquiry's progression.
- HMRC's enquiry co-ordinator may be a useful liaison point.

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- disclose any irregularities of which the business may be aware (if HMRC has not raised any specific risks at this point it may still be possible for a disclosure to qualify as unprompted);
- elicit from HMRC the risks perceived to be present, such as why the business was selected for enquiry. This can enable the enquiry to start to focus on specific risk issues; and
- have an initial discussion about the scope of any required records review focused on specific risk issues.

Some of the early cross-tax enquiries included instances of HMRC showing reluctance to disclose perceived risks. As a result, businesses were less minded to co-operate because they could not understand the purpose of the enquiry. Such situations can result in an awkward stalemate before any progress can be made. More recent experience is that openness about the perceived risks has enabled early collaboration and faster progression of the enquiry.

### Risks to be worked

After the meeting, HMRC will issue a letter confirming the risks it wants to be worked and to request information it proposes to review. Collaboration at this point will be key to the future progress of the enquiries. HMRC may identify several risk issues to be worked across all taxes and may request a lot of information. When considering this request the business may believe that providing what HMRC wants may not be the best approach to reviewing any risk issue. The business therefore has the opportunity to suggest different records or ways of checking a risk.

Agreeing a mutually acceptable approach to working risks at this early stage can save both HMRC and the business considerable time and cost as well as promote joint ownership of the process for the remainder of the enquiry. This requires a degree of trust on both sides. A business that intends to frustrate a reasonable request for relevant information forfeits trust and is likely to receive a formal notice for the provision of information or documents from HMRC (FA 2008, Sch 36 pt 1).

At this stage, HMRC should also issue an action plan including a summary of the risks with proposed completion dates for next steps and an overall target resolution date for the whole enquiry. This is a useful project management tool providing focus on deadlines, which can be absent from other types of enquiry, where it can seem there is no apparent end date.

### Data testing

A built-in feature of cross-tax enquiries is an amount of systems, process and data testing. HMRC will want to gain some comfort about the quality of record-keeping generally, as well as the specific risks identified.

Not all data testing has to be undertaken by HMRC: although it has the technical capability, it does not have unlimited resources. HMRC has confirmed that the scope of any data analysis can be agreed and undertaken by the business or its advisers with the findings shared with it to check.

### Progression to resolution

Provision of relevant information to allay HMRC's concerns about risk should result in early resolution of issues and removal from the action plan. HMRC's activity in cross-tax enquiries is intended to be proportionate. Considering all taxes together in one enquiry has some sense to it, but the business may feel it is being hit from all angles at once.

HMRC resources cross-tax enquiries by appointing a co-ordinator to act as a senior project manager. These are experienced officers and are useful to liaise with.

HMRC should focus on the year of enquiry but, if irregularities are found that could affect earlier years, it will consider issuing discovery assessments (TMA 1970, s 29 and s 30B; FA 1998, Sch 18 para 41).

If HMRC is provided with the relevant information and finds no irregularities, a closure notice should be sought confirming that no adjustments need to be made to the company or directors' personal self-assessments.

If irregularities are found, early disclosure and provision of information to quantify additional tax liabilities can mitigate penalties for failure to take reasonable care (FA 2007, Sch 24 para 9). A useful feature of the regime is suspension of penalties if a business can demonstrate compliance improvements have been implemented (FA 2007, Sch 24 para 14).

The interaction of the various business and personal taxes can complicate administration of any settlement. It is possible to achieve a settlement either by HMRC raising assessments, or by entering into a contract with the business to cover tax, interest and penalties. Agreement in principle of the settlement position can be considered with the HMRC enquiry co-ordinator, but will be subject to final agreement through HMRC governance procedures.

### Joint ownership is key

The key to efficient progress and resolution of the enquiries is to work collaboratively with HMRC:

- Using the opening meeting for HMRC to gain an understanding of the business and how tax risks are managed.
- Requesting HMRC is transparent about the reasons for the enquiries and the risks HMRC believes require checking.
- Developing a joint action plan with mutually agreed work-streams and timetable with a reasonable target resolution date.
- Undertaking reassurance work such as systems/data analysis which can be checked by HMRC.
- Liaising with the HMRC enquiry co-ordinator so ensure work undertaken is proportionate.
- Early disclosure of irregularities, provision of information, quantification of additional tax due and implementation of compliance improvements to mitigate potential penalties. ■

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