Tipping the scales

How is HMRC faring in its mission to strike the right balance between its powers and taxpayer safeguards? Robin Williamson reports

In evaluating the implementation of powers and safeguards introduced since 2012, HMRC has undertaken to abide by 21 commitments to improve its performance.

The evaluation measured how far the new powers and taxpayer safeguards accord with the principles set out in Modernising Powers, Deterrents and Safeguards ("the Powers Review") carried out between 2006 and 2012.

But this exercise missed an opportunity to assess the underlying policy, which in some cases – notably the effect of the Requirement to Correct (RTC) legislation on unrepresented, low-income individuals – has departed a very long way from the Powers Review principle to support those who seek to comply but to come down hard on avoiders.

Evaluating HMRC's implementation of powers and safeguards

The publication of HMRC's report Evaluation of HMRC's implementation of powers, obligations and safeguards introduced since 2012 on 4 February 2021 followed a lengthy consultation which was begun by the Financial Secretary to the Treasury, Rt Hon Jesse Norman MP, announcing on 22 July 2019 that he had asked HMRC "to evaluate the implementation of powers introduced since 2012 in relation to the powers and safeguards principles, engaging with stakeholders, including taxpayers and their representatives".

For some years there had been a prevailing sense that the balance between HMRC powers and taxpayer safeguards was tilting too far in favour of the former. In its report The Powers of HMRC: Treating Taxpayers Fairly, the House of Lords Economic Affairs Committee concluded that pressure on HMRC to crack down on aggressive avoidance and deliberate evasion, necessary though that was, had left it with insufficient resources to fulfil its obligations to treat taxpayers fairly and in accordance with the Charter. The drive to tackle avoidance and evasion with diminishing resources, their Lordships said, had meant that the principles set out in the Powers Review, when HMRC sought to update and modernise the powers of the merged department, were being forgotten.

Echoing those principles, their Lordships said "there is a clear difference in culpability, for example, between deliberate and contrived tax avoidance by sophisticated, high-income individuals, and uninformed or naïve decisions by unrepresented taxpayers", and the Government should make a clearer distinction between the two in its rhetoric on tax avoidance. A similar theme emerged from Sir Amyas Morse's independent review of the policy and implementation of the loan charge (also December 2019) which considered the extent to which the loan charge, despite something like it being necessary to ensure that everyone paid their fair share of tax, prompted serious questions about how proportionate it was in terms of its design and effect on individuals. He concluded that "elements of the loan charge went too far in undermining or overriding taxpayer protections".

In its evaluation report, HMRC concluded that "overall… the approach to implementing powers introduced since 2012 has been broadly consistent with the 2005-2012 Powers

Review principles", while being clear that it was the implementation of the post-2012 powers, not the policy underlying them, that was being evaluated.

HMRC's 21 commitments

Nevertheless, HMRC has acknowledged that in some instances brought to their attention "more could have been done to demonstrate that taxpayers' circumstances had been understood and taken into account when difficult decisions that affected them were made".

The evaluation sets out 21 commitments that HMRC has undertaken, which include matters such as:

- reviewing, updating and where appropriate revising guidance on taxpayers' rights and obligations in respect of various powers;
- exploring ways to improve awareness of HMRC's internal governance processes, especially with regard to anti-avoidance measures such as the GAAR, accelerated payment and follower notices, and the RTC legislation;
- improving some of HMRC's compliance communications, such as letters sent during an enquiry;
- better supporting those in financial hardship;
- improving the experience of taxpayers who correct their tax through the Worldwide Disclosure Facility;
- also improving HMRC's engagement with hard-to-reach audiences through working with voluntary and community organisations, and aspects of customer experience particularly where taxpayers need extra support; and
- reviewing and updating guidance on reasonable excuse and building consistency of approach internally.

When ignorance of the law can be a reasonable excuse

What the evaluation says about HMRC's application of the reasonable excuse defence to the charging of certain penalties is of particular interest in the context of recent case law.

What was once thought to be a hard and fast principle has now been modified by the Upper Tribunal in Perrin v HMRC [2018] UKUT 156 (TCC). Paragraph 82 of that judgment reads as follows:

"One situation that can sometimes cause difficulties is when the taxpayer's asserted reasonable excuse is purely that he/she did not know of the particular requirement that has been shown to have been breached. It is a much-cited aphorism that 'ignorance of the law is no excuse', and on occasion this has been given as the reason why the defence of reasonable excuse cannot be available in such circumstances. We see no basis for this argument. Some requirements of the law are well-known, simple and straightforward but others are much less so. It will be a matter of judgment for the [First-tier Tribunal] in each case whether it was objectively reasonable for the particular taxpayer, in the circumstances of the case, to have been ignorant of the requirement in question, and for how long."

In brief, ignorance of the law can be a reasonable excuse if the taxpayer's ignorance, viewed objectively, was reasonable given the taxpayer's particular circumstances or attributes.

In a later First-tier Tribunal case, Jacques v HMRC Commrs [2020] UKFTT 311 (TC), the judge followed the Upper Tribunal in Perrin in finding that the appellant, a PAYE taxpayer with no experience of self-assessment, had a reasonable excuse for not submitting a tax return to notify his liability to the High-Income Child Benefit Charge (HICBC) until “nudged” by HMRC. The judge, while acknowledging that HMRC had no obligation to notify every taxpayer of every change in the law that might apply to them, said that, equally, the taxpayer is not obliged to “go rummaging through all HMRC’s information on the off-chance that there might be something which is hidden away in it which is relevant to his tax position”.

How HMRC implements reasonable excuse

And yet, evidence submitted by the Low Incomes Tax Reform Group to the evaluation contains a case history where a low-income taxpayer unwittingly fell foul of the RTC rules and ended up with a penalty. This is cited as Example 1 in the evaluation report (on page 20):

“Mr A first received his overseas pensions in 2007, while resident in the Netherlands, and paid tax on it to the Dutch tax authority. He moved to the UK in 2010 and took up full-time employment. As a result, his total taxable income exceeded the UK personal allowance from 2010/11 to 2012/13 and under UK law he should have notified HMRC about the pension and paid UK tax on it. HMRC wrote to Mr A in April 2019, after receiving information from the Dutch tax authority about his overseas pension income. Mr A told HMRC he did not realise his overseas pension might be taxable in the UK, and contacted Tax Help for Older People (THOP) for help. THOP argued Mr A had a reasonable excuse for failing to comply with the [Requirement to Correct (RTC) legislation] because he thought that the pensions being sourced overseas and having overseas tax deducted meant they were taxable overseas and not in the UK. He was also unaware if he had any obligation under RTC, because he thought he was compliant. HMRC did not agree that Mr A’s circumstances constituted a reasonable excuse. As a result, THOP said Mr A paid £3,334 in tax, interest and penalties, including penalties of £1,809 for failing to comply with the RTC. THOP then requested HMRC remit the debt. HMRC can only remit debt in very limited circumstances and instead agreed a time to pay arrangement over three years. THOP said this is causing the taxpayer financial hardship.”

The published evaluation is ambivalent as to whether it was right or reasonable to turn down a plea of reasonable excuse in the circumstances of that case, given that a reasonable excuse defence is allowed by the RTC legislation and HMRC simply chose not to apply it. But it does report the view of the tax agents on the consultative forum that HMRC could have done more to ensure such taxpayers were aware of their obligations. Few ordinary taxpayers have heard of the RTC legislation and fewer still have any intention of evading or avoiding tax by hiding activities, income or assets offshore. Mr A’s is not the only such case cited in the evaluation – the Tax Investigation Practitioners Group contributed a similar story in Example 19 (on page 45).

As the RTC legislation is aimed at egregious avoidance and evasion, the penalties are severe – 200% of the potential lost revenue, mitigable to 150% in the case of prompted disclosure. Hence the exceedingly large penalties element in Mr A’s settlement figure in the example above.

The evaluation report was clear that it was only intended to cover implementation, not the underlying policy – but to operate a policy that imposes 150% tax-geared penalties on people like Mr A for mistakenly thinking that their income is taxable in the country where tax has been automatically deducted is not only harsh, it is quite contrary to the Powers Review principle to “support those who seek to comply but come down hard on those who seek an unfair advantage through non-compliance". In the RTC legislation, the tax authority has come down equally hard on the innocent and the guilty, and HMRC's approach to implementing the rules provides no mitigation in these cases.

Conclusion

Hard cases make bad law. It is good that the evaluation has taken place and that HMRC has signed up to the 21 commitments to improve their implementation of the post-2012 powers. But, as the LITRG spokesman acutely observed, the evaluation report is worth nothing on its own without a genuine and concerted effort by HMRC to act on their 21 new commitments. No doubt HMRC will do its best on the implementation.

However, the failure to evaluate the underlying policies has missed at least one opportunity to correct the skewed balance between pursuit of the avoider and support for the naturally compliant in the egregious way in which the RTC legislation bears down upon innocent mistake. Penalty levels which can go no lower than 150% of potential lost revenue for prompted disclosure, or 100% for prompted disclosure, are a far cry from Powers Review inaccuracy or failure-to-notify penalties, which can be reduced to as low as zero for unprompted disclosure even where there is an offshore element. But matters of underlying policy takes us into the political arena, in which HMRC is less influential than certain other organs of government. Tax practitioners who care about such matters should write to their MP.

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