HMRC letters: ‘Your offshore assets, income or gains’

Kugan Panchalingam and Helen French discuss HMRC’s increasing use of so-called nudge letters to prompt taxpayers into paying more tax

We continue to see our existing clients receiving these ‘nudge’ letters, as well as receiving enquiries from prospective clients who have been filing their own tax returns or were represented by another tax advisor.

International Exchange of Information

Before discussing the ‘nudge’ letters in detail, it is helpful to understand where the information prompting them is coming from, and why.

These stem from a much wider programme which provides for the Automatic Exchange of Information (AEOI) specifically targeted at tax evasion on a global scale. To date, over 90 countries have committed to this programme by signing international agreements to facilitate the exchange of financial information between tax authorities.

A list of reportable jurisdictions is given in the HMRC International Exchange of Information Manual, at IEIM402340, with additional countries signing up regularly.

The overarching standard for this information exchange is the Common Reporting Standard (CRS), which defines ‘reportable accounts’ and ‘reportable persons’ in detail.

Broadly, reportable accounts include those held with banks, building societies, insurance and investment companies. A reportable person is an individual account holder linked to the country receiving the information (i.e. to the UK for HMRC purposes) in such a way as to suggest they may be taxable in that country (UK resident, or non-resident but with UK accounts for example).

All financial exchange agreements require the following basic information to be provided:

- individual’s name, address and tax reference;
- the account number and balance at the end of the calendar year (or other agreed date);
- jurisdiction to which the information is reportable; and
- name and identifying number of the financial institution.

Some agreements require additional information, e.g. the individual’s date and place of birth (particularly the US under FATCA and UK agreements with Crown Dependencies and Overseas Territories).

The majority of agreements are reciprocal and HMRC will both receive and provide information with the counter-party jurisdictions. Non-reciprocal agreements, signed with those territories that do not have income tax, only provide information to HMRC.

In summary, these agreements mean that HMRC receives a huge amount of financial data on individuals annually from overseas reporting institutions and is able to compare that with what taxpayers are reporting in their self-assessment returns, as well as identifying UK residents who do not appear to have reported at all.

The new ‘nudge letters’

Most recently, HMRC appeared to be sending these letters to individuals resident in the UK who had a financial connection to India, suggesting they have been exchanging information with the Income Tax Department of India. In the enquiries that we have seen it was apparent that most individuals that received the letters had for one reason or another not reported the interest arising on bank accounts held in Indian banks, which HMRC has now become aware of.

We expect that this trend will continue for the foreseeable future given the number of countries already signed up to exchanging information under the CRS, and it will take HMRC some time to crunch through the vast volume of information they are receiving.

Originally, it appeared that HMRC were sending out these ‘nudge’ letters on a speculative basis, and receiving a letter did not necessarily suggest that a mistake or omission had occurred. However, their approach now appears to have changed.

In the latest version of these letters HMRC have specifically stated that “We have compared the information we have received with your tax record and tax return(s). We believe that you may not have paid the right amount of UK tax. There may be a reasonable explanation for this.” This wording suggests a more risk-based approach undertaken and some data comparison has been done.

HMRC’s capabilities are ever developing in this area and the global information exchange system is becoming increasingly sophisticated and streamlined.

Nevertheless, the responsibility rests with taxpayers to ensure their tax affairs are up to date and that professional advice has been sought where appropriate, as has always been the case.

What to do if you have received a letter?

In line with the CIOT guidance we encourage individuals not to sign the certificate of tax position as there is no legal requirement to do so. Furthermore, the letter does not reference a specific tax year to which the 'offshore income or gains' relate, but the certificate includes provision to state specific years when responding: "…I believe I have declared all my overseas income and/or gains correctly on my tax return(s) as shown below…"

Previous versions of the letter did not specify a tax year, nor ask the taxpayer to do so, whereas this version puts the onus on the taxpayer to do that. The risk of accidentally making a false declaration here is therefore significant.

Regardless, some kind of response must be submitted as otherwise HMRC may be prompted to raise an enquiry. We can advise individuals on how to respond to HMRC, regardless of whether:

- nothing further needs to be declared; or
- a disclosure needs to be made.

If it turns out that the individual should make a disclosure, a decision needs to be made on which channel would be the most appropriate given the individual's circumstances.

The letter specifically states that 'you must register with the Worldwide Disclosure Facility'; however, this is not strictly correct. There are various other disclosure channels the individual can use, so the WDF is not always the most appropriate. For example, the client may still be able to amend prior year tax returns if they are within the statutory time period, or it may be in their best interest to enter into a disclosure through the Contractual Disclosure Facility (COP9) where fraud was involved.

Another issue that we suspect that this is probably going to be the reason for any deemed irregularity in many cases, is that the format in which HMRC receive information from other countries is not necessarily aligned to the UK tax year. The majority of countries have a calendar tax year, whereas in the UK the tax years runs from 6 April to 5 April.

Therefore, UK domiciled individuals, or non-domiciled individuals who file on the arising basis of taxation, may have declared and paid tax on their worldwide income and gains, albeit split across two calendar years and so HMRC are not comparing like for like.

Furthermore, non-domiciled individuals who do elect for the remittance basis of taxation are not required to have reported their foreign income and gains unless such funds were remitted to the UK.

Finally, another issue we have seen arises for individuals holding accounts in the capacity of nominee or as trustee of a bare trust. The taxable person in those instances is likely to be the beneficial owner, rather than the account owner, however the information provided to HMRC does not always make that distinction, at least not clearly enough.

Consequences of undeclared income and/or gains

The Requirement to Correct legislation (RTC), found at Section 67 and Schedule 18 of the Finance (No. 2) Act 2017, created an obligation on taxpayers with offshore irregularities to disclose the relevant information to HMRC by 30 September 2018; this date deliberately coincided with the date on which more than 100 countries started to exchange financial account information under the Common Reporting Standard.

Only tax non-compliance committed before 6 April 2017 falls within RTC. Where the normal assessment window for those years would expire between 6 April 2017 and 5 April 2021, the window was extended to the later of 5 April 2021 or the ordinary assessment window that would apply.

For example, the assessment window in respect of 2011/12 (in a case where the taxpayer was careless) would ordinarily run out at midnight on 5 April 2018. However, under RTC, HMRC would have been able to raise an assessment in respect of that year on 6 April 2017, so the window extends to 5 April 2021.

Anyone who did not regularise their affairs by September 2018, or at least submit a notification to HMRC that they intended to correct their prior non-compliance, is now within the draconian Failure to Correct (FTC) regime.

For tax liabilities up to and including 2015/16 HMRC will assess penalties of 200%, which can be reduced down to 100% (or 150% if the disclosure was prompted by HMRC) and no more, unless the individual can prove that they have a reasonable excuse for their failure to notify HMRC of chargeability to tax or to correct an inaccuracy in their tax return involving an offshore matter.

Furthermore, the following additional penalties may also apply:

An asset-based penalty: Where the tax liability exceeds £25,000 and the individual deliberately failed to comply. This penalty is 10% of the value of the asset in respect of which the deficiency in tax arises.

Offshore asset moves penalty: Where HMRC can prove that the individual moved assets to ensure that their details are not reported to HMRC under any of the international information exchange agreements. This penalty can be up to 50% of the standard penalty and is charged in addition to that penalty. It only applies to asset moves that took place on or after 26 March

2015.

Naming and shaming by HMRC: In the most serious of cases HMRC may publish details of the offender online if the tax deficiency exceeds £25,000 per investigation. Again, this can only apply where the deficiency was caused by a deliberate action taken by the individual.

Summary

Given the complexities of the UK tax legislation, particularly in respect of offshore matters, we encourage all relevant individuals to review their tax affairs regularly to avoid a potentially unwelcome outcome.

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