

Furlough fraud: what's HMRC to do?

Salman Anwar and Haris Rehman explore abuse of the government's job retention scheme and analyse HMRC's response to it

23 March 2020 – the day when Britain went into full lockdown.

Numerous sectors of the economy were hit hard with the hospitality sector perhaps one of the hardest hit. Businesses had to close at very short notice leading to a huge amount of uncertainty for them and their employees. Once bustling city centres were left deserted. Businesses and jobs were at risk and just when all hope seemed lost, Mr Sunak, like a knight in shining armour, announced a whole raft of measures to help stabilise the economy. The Coronavirus Job Retention Scheme (CJRS), also known as the furlough scheme, was the flagship measure designed to protect jobs and support a huge proportion of the population economically.

The scheme was initially set to end on 30 June 2020 but was later extended until 31 October 2020, with the introduction of flexible furlough.

The initial scheme enabled employers to receive up to 80% of their furloughed employees' wages from the government in the form of a grant, up to a limit of £2,500 per month per employee.

The furlough scheme was akin to a castle into which the knight, Sunak, invited vast swathes of the population to take shelter and seek protection from the invading hordes in the shape of the virus and the economic uncertainty that accompanied it.

The results of the scheme in protecting jobs, at least in the short term, speak for itself with the British Chamber of Commerce noting that since March, the scheme has been used by two thirds of British businesses supporting approximately 9.6 million jobs.

But, like the medieval knight of yore, the Honourable Sunak could not defend his castle without the aid of a stout body of yeomen – and in this case, he enlisted the help of HMRC to shore up the defences of the castle ensuring the (furlough) gates of the castle were well guarded. The rules – which have come in for some criticism – allowed only those were thought to be deserving of support to be invited in. HMRC performed their duties in their usual diligent manner, putting guards at the gates, digging a deep moat around the castle walls and erecting a drawbridge.

While this was implemented in “unprecedented times” and at great speed it was recognised by the powers that be that it would be wiser to carry out checks on those who were being allowed to enter rather than attempting to check them after they had been let in. However, time was of the essence and, as the invading virus came closer, HMRC was obliged to process large crowds of clamouring citizens within a matter of days. Even then, the need was so urgent that queues formed outside the castle.

As Mr Harra, CEO of HMRC, told the PAC in September, HMRC were obliged to focus on turning away organised criminals rather than legitimate employers about whom HMRC may have had concerns.

Given the circumstances it is perhaps understandable that certain undeserving citizens were able to take refuge in the castle and overstayed their welcome. Mr Harra told the PAC that HMRC’s hotline and online reporting tool had received 8,000 reports of suspected furlough fraud by the public and HMRC had subsequently identified about 27,000 “high-risk” claims. Mr Harra told the PAC that HMRC would write to those claimants giving them an opportunity to “correct” their claims. He also told the PAC that about 10,000 of the identified claims are expected to be investigated by HMRC.

With HMRC paying out approximately £35bn in claims to the end of July and estimating that between 5-10% of this to have been overpaid as a result of fraud or error, this equates to potential fraudulent claims of between £1.75 billion and £3.5 billion. Given these numbers, it is easy to see why the government wants to find those who have abused the hospitality of the castle and charge them for their stay. The Government has already given time to make corrections to those that submitted erroneous claims in the initial phase, however, that time will shortly run out (20 October 2020). HMRC is now expected to send the soldiers out of the barracks to deal with those who it suspects of having fraudulently claimed CJRS grants. In performing this task, HMRC’s foot soldiers have a number of weapons in the armoury.

Potential types of fraudulent claims

While HMRC had some very good defences, including checking that the employee was on the payroll and had been included in a PAYE submission prior to the announcement of the scheme, its attention was focused on keeping out the most unwanted and organised criminals.

Here is a non-exhaustive list of how employers may have fraudulently claimed for amounts they were not entitled to:

- Claiming on behalf of an employee without their knowledge while the employee continued to work as normal.
- Placing employees on furlough and then requesting that they continued to work as normal.
- Setting up another company to operate the business while furloughing staff through the original company.
- Subcontracting the services of the employees to another firm while they were furloughed by the original employer.
- Claiming on behalf of employees who did not exist.
- Claiming on behalf of ex-employees who no longer worked for the employer.
- Using furlough grants to pay for redundancy payments.
- Claiming furlough payments and not passing on all of the grant to the employee.
- Claims calculated using inaccurate factors such as hours worked, etc..

The above list is clearly focusing on those who would have knowingly overclaimed but it is worth bearing in mind that it is widely acknowledged that the calculation of grants was complicated and that genuine errors could easily have been made. However, the legislation requires employers to correct any error where they (whether knowingly or unknowingly) overclaimed at the time of making the claim or if a later change in circumstances lead to the original claim becoming excessive.

The number of potentially fraudulent claims predicted by HMRC is a sobering one but unfortunately, many in the tax profession had predicted there would be widespread abuse of these support measures. So, the key question, and the crux of this article is, how is HMRC's going to deal with these fraudsters?

HMRC's response

To mix our metaphors freely, after a period of guarding the front door HMRC are now firmly out in the countryside searching for those who have played the system.

HMRC had always anticipated there would be some suspected fraudsters

who would try to abuse the scheme and would succeed in this aim. Thus, HMRC focused on proactively stopping the fraudsters at the front door before the funds were released. After all, it is always easier to stop a payment rather than having to claw it back. However, with the sheer number of claims, it would have been an administrative impossibility to triage each and every individual claim and there were always bound to be some false claimants that would slip through.

Those that did slip through the net have been given the opportunity to either disclose their fraud to HMRC voluntarily or risk being investigated criminally or using civil powers. However, it is clear that HMRC are not hanging around and have carried out a number of arrests and have also begun other criminal and civil investigations into suspected fraudulent furlough claims. The well-publicised arrests of a businessmen in the West Midlands, an accountant in Romford and a company director in Walthamstow for alleged furlough fraud are a timely signal that HMRC are intent on winning this particular battle.

The first and most relevant (civil) power that HMRC have been given is that any overpayment will be subject to a 100% tax charge on the employer. Failure to correct any errors or overclaims by the period set by HMRC will make the employer liable to a potential penalty of 100% of the amount overclaimed under the failure to notify provisions, as amended by The Finance Act 2020. Put simply, as a start point, a fraudulent claimant will be expected to pay 100% of the amount overclaimed and potentially up to twice what they claimed.

Another, perhaps lesser publicised power, but one which is seeing increased use is Account Freezing Orders (AFOs). This power is contained within the Proceeds of Crime Act (POCA) as amended the Criminal Finance Act 2017 and enables HMRC to apply to a Magistrate for an order freezing the bank accounts of the suspect .

Even before the COVID19 pandemic, HMRC had begun utilising AFOs on with an ever-increasing frequency. HMRC issued 166 AFO's in 2019/2020, which was an increase of 177% from the previous year. A recent "Asset recovery statistical bulletin" published by the Home Office reveals that in 2019/20 a total of £208 million of funds across 812 bank and building society accounts were subject of restraint under AFOs. The figures for the previous year were £94 million and 740 accounts, respectively.

HMRC admitted in the recent PAC hearing that it cannot realistically catch up on the number of new enquiries it normally opens, which had

fallen due to the COVID19 related pause in HMRC's compliance activities. HMRC has said that, to make up, it will focus on areas where it can make a difference. As a consequence, suspected furlough fraud will be even higher on the lists of areas to focus on than it already was and it is expected that the use of AFO's will see a continued increase as it will be the quickest way for HMRC to stop the proceeds from suspected fraudulent claims from disappearing.

HMRC views AFOs as a very effective tool to ensure that the proceeds of unlawful conduct do not dissipate while it carries out an investigation. One of the advantages for HMRC is that these orders are relatively easy to obtain. HMRC has told us that it has internal checks and balances for use of AFOs and only certain trained officers within HMRC are allowed to use these. However the bar for obtaining an AFO is relatively low and all HMRC need to demonstrate to a Magistrates in order to obtain an AFO is that they have reasonable grounds to suspect that money is recoverable property or is intended for use in in unlawful conduct (both terms normally used in criminal rather than civil proceedings).

After HMRC has completed its investigation it can ask for the amounts suspected to be recoverable property to be forfeited. It can also apply for a Forfeiture Notice to the courts.

While we would not disagree with the need to go after suspected fraudsters, we would caution that a very low threshold seems to have been set for such a draconian power. The consequences of such an order being incorrectly imposed on an innocent person or their business would likely be catastrophic. To go back to using metaphors, the concern is that the yeomanry have been authorised to use flame throwers to search the fields, and are in danger of burning down the farmhouse and the village

The fear with such a powerful tool at HMRC's fingertips is that the relative ease of obtaining an AFO could result in innocent taxpayers who have done nothing worse than make an honest mistake, having their accounts frozen. These accounts can be frozen for up to two years and the individual is left with no way of paying their monthly expenses such as mortgages, bills, etc.

In theory only a specified amount in the account is subject to the freezing order but given the nature of the power and the suspicions involved, account holders have found it very hard to access the excess funds in the account. As will be appreciated, the very fact that a person has been subject to such an order can be catastrophic for their

commercial reputation, let alone their subsequent borrowing facilities! We understand that HMRC are working with the banks to resolve this particular aspect and it is commendable that they have recognised this as an issue but nonetheless it remains an area of serious concern.

We recently raised our concerns with HMRC regarding the use of AFOs and specifically that these could serve to dissuade people from making voluntary disclosure if these were inappropriately used. We understand that HMRC have no operational plans to use these where someone wants to make a voluntary disclosure.

A further, and relatively new power, that has been granted to HMRC is that of making directors of an insolvent company, in circumstances involving tax avoidance and tax evasion, to be held joint and severally liable for amounts payable by the company to HMRC. This includes the 100% tax charge in respect of furlough overclaims. The legislation is contained in Schedule 13 of the Finance Act 2020.

In conclusion, HMRC has a whole raft of weaponry to combat those it suspects of CJRS fraud. However, as those well acquainted in dealing with HMRC's investigation can attest, the line between legitimate errors and what HMRC considers to be deliberate or fraudulent conduct can often be badly blurred. Employers who fear that they may have made a mistake need to take active steps and seek appropriate professional advice to rectify this as soon as possible. A failure to act after becoming aware of an error is not viewed kindly by HMRC and can in itself be considered fraudulent conduct.

To return to our opening analogy, the castle is now being swept by special forces and their mission is to seek and recover/destroy. Anyone who has overclaimed, intentionally or otherwise, should also seek professional representation and make a voluntary disclosure as soon as possible. The consequences of not doing so could well prove fatal to your financial health.

- Salman Anwar is a Senior Manager in Mazars Tax Investigations team having previously been a Tax Inspector having worked in HMRC's Fraud Investigation Service. Salman can be contacted on 073 9444 8889 or salman.anwar@mazars.co.uk

- Haris Rehman is an Assistant Manager in Mazars Tax Investigations Team having previously worked in HMRC's Fraud Investigations Service. Haris can be contacted on 073 9939 9976 or haris.rehman@mazars.co.uk