

ESS under renewed HMRC focus

Sarah Mawson and Varoon Saccaram explain what hospitality and retail businesses receiving an HMRC ESS nudge letter need to do next. Just don't ignore it...

Past attempts to tackle users of electronic sales suppression (ESS) tools have been relatively ineffective but HMRC has recently assigned its Fraud Investigation Service to the task of challenging suspected users. This article explains what this means for implicated traders in the hospitality and retail sectors – and what to do next. Within the four walls at HMRC, it has been an old adage that “a prevalence of cash usually equates to a fruitful tax enquiry”. Consequently, businesses operating in hospitality and retail sectors have traditionally been subject to more than their fair share of investigations. Even today, despite the use of ‘physical cash’ becoming sparser, the spotlight still remains on these sectors. This is largely due to HMRC’s discovery of ESS tools being used to manipulate sales records and artificially suppress tax liabilities.

What is electronic sales suppression?

Where a business uses a device (software or hardware) to manipulate electronic sales records to support an incorrect tax return, HMRC will consider the business to be engaged in electronic sales suppression.

For example, a business using an ESS tool might make a sale for £10, with the customer paying by card. The business would receive the full £10 payment. However, when the sales records are produced, that £10 sale might have been recorded as a £5 sale or even omitted from the sales record altogether. When those sales records are used to prepare accounts and tax returns, the ESS tool will have effectively provided a false accounting record to artificially lower a trader’s tax bill.

HMRC’s developing approach to ESS-related fraud

HMRC first identified use of ESS tools during the pandemic when some businesses were discovered to be using such devices to embellish their claims to the Coronavirus Job Retention Scheme. Eventually, HMRC’s investigation work identified the suppliers of these ESS tools which, in turn, enabled HMRC to track all businesses who had purchased such tools.

In late 2022, HMRC issued a series of targeted ‘nudge’ letters to businesses it suspected of having purchased ESS tools. These nudge letters made the businesses aware of HMRC’s suspicions and this was meant to encourage them to come forward and make a voluntary disclosure.

The campaign didn’t have the desired effect, with around only one in seven businesses responding to the nudge letter. HMRC’s position is that it has received

considerably fewer disclosures than anticipated and that, consequently, it has spent significant time formulating a new plan to tackle suspected users of ESS tools. This new approach will be led by its elite investigation office, the Fraud Investigation Service (FIS). While it is not yet clear whether FIS will be opening investigations immediately, or providing businesses with a second opportunity to make a voluntary disclosure, there's no doubt that HMRC will be taking more robust further action in the forthcoming future.

Effect on hospitality/retail

At first glance, the vast majority of hospitality and retail businesses are unlikely to be affected by the resurgent focus on tackling ESS-related fraud. It is likely that HMRC's approach will be extremely targeted and directed specifically at those where it already possesses information that suggests an ESS tool was purchased. For the small number of traders who may be implicated by the data that HMRC holds, there is thus a real and pressing need to consider how to best protect themselves. HMRC is able to utilise its 'information powers' within its armoury to help it check the accuracy of a taxpayer's position. These information powers are robust and, while certain taxpayer safeguards exist, where HMRC has reason to suspect a loss of tax it is foreseeable that HMRC will use these powers to inspect documents and 'raid' business premises. These HMRC actions can occur without any prior warning to the business and even when the business's tax affairs appear to be in order. It is suspected that with this renewed focus, HMRC's starting position will be to consider that anyone identified as a purchaser of an ESS tool will have done so with the intention of manipulating business records to suppress their tax liabilities. The courts have consistently found that where an individual has knowingly and intentionally failed to comply with their tax obligations, it is an act of tax fraud. This fact, coupled with the active involvement of the Fraud Investigation Service, demonstrates a real prospect of HMRC conducting investigations with a view to prosecuting those who have used ESS tools to gain a tax advantage.

Protection through voluntary disclosure

While HMRC continues to operate a disclosure facility specifically for ESS, it is vital that the vast majority of ESS tool users consider making use of HMRC's Contractual Disclosure Facility (CDF).

Making a full and accurate disclosure through the CDF is the only way for implicated individuals to secure immunity from the prospect of criminal prosecution at a time where HMRC are buoyant following their recent success in the courts with Bernie Ecclestone.

What actions should businesses take?

Existing tax advisors who are aware of their clients who have previously received a 'nudge' letter from HMRC that the business owner didn't act upon have a more

pressing need than most. These businesses are strongly advised to seek professional representation and to inform their advisers of any ESS tools they have previously utilised. For their part, advisers will be able to provide recommendations based on the facts of each case and guide them through the most appropriate HMRC disclosure facility.

For those who haven't previously received an HMRC nudge letter, the advice remains constant. HMRC has confirmed that it didn't issue nudge letters to every business it suspected of using ESS tools. So if a business hasn't previously heard from HMRC it doesn't mean that they have slipped under the radar. Arguably, it is those traders who haven't previously heard from HMRC who stand to gain the most by coming forward voluntarily. Any businesses approaching HMRC to make an unprompted, voluntary disclosure to HMRC will have the ability to secure a reduced overall settlement.

Regardless, if a taxpayer is in any doubt whatsoever as to the accuracy of their tax affairs and whether they may be implicated by the data HMRC holds, it is strongly recommended that they seek professional advice. HMRC offers a myriad of disclosure facilities, all with their own nuances and requirements. Tax dispute professionals deal exclusively with HMRC investigations and disclosures, and will ensure that taxpayers obtain the necessary support to regularise their tax affairs in an appropriate way, without exposing them to unnecessary tax, interest or penalties.

While the use of ESS tools is a relatively new phenomenon, Grant Thornton's tax dispute resolution team has represented several clients who received HMRC's initial tranche of nudge letters. We understand how HMRC conducts these investigations and our experts are well equipped to guide you through the process. Our team includes several former senior HMRC FIS officers, meaning we understand exactly how to handle investigations and disclosures in a manner that protects clients from the threat of criminal prosecution.

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