HMRC disclosures: getting it right

Mala Kapacee highlights areas to keep in mind when choosing a disclosure route, making the disclosure and communicating with HMRC after submission

Disclosures to HMRC are a way of letting the department know when there is an under-declaration of tax. A disclosure to HMRC must be complete and correct. This means that it must include all instances of under-declaration of tax known to the client subject to the relevant time limits.

In the same way that HMRC is governed by time limits for raising assessments, so the same time limits govern the period(s) the disclosure must cover. This means that a person who has taken reasonable care with their tax returns would only need to go back four years; while someone who failed to take reasonable care needs to go back six years, etc. Be aware that the time limits are extended if the disclosure relates to tax arising from overseas assets.

For failure to notify, the time limits are different again. If the failure to notify was due to the taxpayer's 'negligent conduct 'or similar by someone acting on their behalf, then HMRC can raise assessments going back the full 20 years unless there is a reasonable excuse.

Why make a disclosure?

Lower penalties: penalties for unprompted disclosures are lower than for those that are prompted by interventions from HMRC. Penalties for careless behaviour can be 0% if unprompted but the minimum is 15% for prompted. For tax arising from offshore assets, an unprompted disclosure can attract a minimum penalty of 100% of the tax due.

Potential immunity from prosecution: under the Contractual Disclosure Facility (CDF), HMRC will formally agree not to undertake an investigation with a view to criminal prosecution provided that the client admits to deliberate behaviour and a full disclosure is made. In practice, with other disclosures, HMRC is highly unlikely to attempt a criminal prosecution unless the disclosure is found to be incomplete on a significant matter. The CDF is the only facility that guarantees this.

Save time (and professional fees): disclosures are time intensive in the short term; however, there is a structure to the process. Once the disclosure has been submitted, it will be accepted if it is complete and correct, the calculations are correct and any assumptions are reasonable. Conversely, if no disclosure is made and HMRC opens an investigation, the process will be driven by HMRC's questions. This is reactive and unstructured leading to a much longer process resulting in more stress, a longer process and higher costs for the client.

Dictate the narrative: when making a disclosure, the client is coming forward and therefore has an opportunity to show themselves in the best light and to present the facts from their perspective. This is easier than trying to persuade HMRC to see things differently once an officer has opened an enquiry with a particular scenario in mind. This is also important for penalties. Further, the fact of making a disclosure automatically demonstrates that the client is engaged in the process and wishes to resolve their affairs, having taken steps to disclose as soon as errors were brought to light.

The alternative

HMRC receives a lot of information from overseas (via the common reporting standard), as well as from a number of other platforms including banks, crypto-asset and digital marketplace platforms, social media and other government departments, including land registry.

HMRC's CONNECT software will also compare data on company and individual tax returns, for example. HMRC may not open an enquiry immediately, but if you have identified an issue the chances are that sooner or later HMRC will catch up with your client. If HMRC has sent out a nudge letter and no response is received they will almost certainly open an enquiry, although how long this takes is uncertain. As mentioned previously, if HMRC open an enquiry the penalties at the end of the process will be higher than if the client had come forward. With respect to deliberate behaviour, 'naming and shaming 'then becomes a risk as well.

Choosing the right disclosure

There are a number of disclosure facilities available. However, the process for making a disclosure is very similar for all of them. The type of disclosure to select will depend on a number of factors, mainly:

- the source of assets giving rise to the tax liability;
- relevant taxes; and
- need for any protection from investigation with a view to prosecution.

The source of assets will determine which team the disclosure goes to. If assets are based overseas, then the Worldwide Disclosure Facility (WDF) is best. If the income comes from let property use that specific facility. Things get more complicated if you are doing a disclosure on rental income from an overseas property or crypto-assets in an overseas account. In these cases, the WDF should be used as usually there is other overseas income in the mix.

Often clients will choose to make a disclosure as a result of a nudge letter from HMRC. These one to many letters cover a number of scenarios – including sale of shares and properties, undeclared dividends and overseas income – and may advise or suggest how to make a disclosure. In cases where there is no recommended route, the type and wording of the disclosure needs to be carefully thought out to ensure only relevant details sufficient to resolve the matter are provided. In all cases with nudge letters, where a certificate is included I recommend not signing the certificate and sending it to HMRC.

Tax fraud is a criminal matter. Therefore, where the under-declaration of tax is a result of deliberate behaviour, the client may be concerned about criminal prosecution. If this is the case, then the only route that affords sufficient legal protection is the CDF, which can be used for all taxes.

The disclosure process

The disclosure process is relatively standard for most disclosures. The client (or agent on the client's behalf) must provide correct tax calculations, and explain to HMRC the basis for these. For disclosures via the Digital Disclosure Service (DDS), completion of the disclosure will include declaration of any 'legal interpretation – ' for example, interpretation of domicile rules, transfer of assets abroad legislation, etc.

The DDS form includes a space for explanation of the source of the assets and the reason for penalty percentages. This space should be used to provide as much detail as possible.

When submitting the disclosure, the client must make an 'offer 'to HMRC of the amount of tax, interest and penalties believed to be due, along with confirmation of their understanding that the disclosure is complete and correct to the best of their knowledge. Submission also confirms acknowledgement that "if the disclosure is found to be false then [the client understands they] may be liable to criminal prosecution".

The Contractual Disclosure Facility

The CDF is offered by HMRC either when a taxpayer is being investigated under Code of Practice 9 (COP9) for serious fraud or if a taxpayer requests a CDF arrangement and HMRC agrees to offer it. HMRC is under no obligation to offer CDF on request and also has no obligation to advise the taxpayer why it was denied.

A request for the CDF will be denied if the taxpayer is already being investigated (whether in criminal or civil proceedings). If HMRC agree to offer CDF, they must first open a COP9 investigation. COP9 is the code of practice applied by HMRC when civilly investigating situations where a taxpayer is suspected of committing tax fraud (normally a criminal offence). HMRC will open an investigation into the taxpayer's affairs and offer them the opportunity to 'come clean 'and make a full disclosure in exchange for a commitment from HMRC not to commence a criminal investigation into areas that are disclosed.

Once HMRC has offered the taxpayer CDF, an Outline Disclosure (OD) must be made within 60 days. The outline disclosure should explain what the liabilities are, who was involved and when the issues arose. For deliberate behaviour, the report must go back 20 years and include all tax discrepancies whether deliberate or not.

Following submission of the OD, there will be a meeting with HMRC to determine the scope of a report detailing the tax issues and computing the liabilities.

When applying for the CDF, aside from the protection against potential prosecution, advisers must consider the wider implications. For certain professions, admission to tax fraud can result in losing a career. If the client does not obtain minimum penalties there is also the risk of naming and shaming – this is particularly relevant to high-profile individuals. Clients need to be made aware of these risks upfront and the process considered accordingly.

Finally, as with all disclosures, incomplete CDF disclosures carry the risk of prosecution. With the CDF, as there is already an admission of deliberate behaviour, the risk is that much higher. The client should be made aware of this and be fully engaged in the process.

After submission

Once a disclosure has been submitted, HMRC will review it and respond. With most disclosures, the aim is for HMRC to respond within 90 days and often the responses are much quicker.

With disclosures under the CDF, responses can take more time as reports are usually more detailed, complex and cover a longer time period. However, you will also have a designated case officer so the process is more streamlined once the report has been reviewed. Once HMRC has clarified all/any outstanding points, penalties will need to be discussed and applied as appropriate.

Initial queries regarding a disclosure will in the first instance be informal. Providing the questions are relevant to the disclosure and no more than clarification there is no reason to withhold answers. However, where the questions go beyond what was covered in the disclosure, advisers should consider whether HMRC is looking at anything else or whether they are simply fishing for more information about the client's affairs.

If the questions appear irrelevant or 'fishing', think about whether to ask for the questions to be issued via a Schedule 36 notice. This will ensure there are certain protections in place and there are legislative provisions for appeal against the notices. The safeguards applicable to Sch 36 notices can still be quoted in respect of informal information requests but HMRC is not bound by them unless the notice is formal.

Be aware that penalties can go up if this is deemed to be non-cooperation (namely, if it is found that questions asked were reasonable and relevant to the client's tax position). Remember that until HMRC formally accept the disclosure, nothing is agreed even though the payment has been made.

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