

It's good to talk

Waqar Shah explains why mediation is very often the best course to take to resolve a contentious tax matter with HMRC

In a perfect world my role would not exist. There would be no need for there to be contentious tax solicitors (or contentious tax advisers of any kind) as it would be perfectly clear to both the tax authority and the taxpayer the amount of tax due in every situation and this would be duly paid. Until we are able to reach this tax utopia, those that are able to help clients navigate the complexities of contentious tax issues are (unfortunately) here to stay. However, part of that process should involve looking at different ways to resolve issues – not just committing the parties to a (potentially expensive) court or tribunal hearing.

It may not be commonly understood, but litigation of any variety can take years to conclude. Tax litigation can include those matters which are both technically complicated but also factually heavy. Therefore, a tax dispute is not immune from potentially needing to go through a few levels of the appellate system, over the course of some years.

In other disciplines, the use of mediation is widespread; it is for that reason that the majority of civil disputes do not reach a courtroom as they are settled beforehand. Indeed, alternative dispute resolution (ADR) is becoming an increasingly efficient manner of resolving such matters, without needing to defer to lengthy, and often costly, tribunal/court litigation.

HMRC's initial decision

Tax advisers across the board will at some time or another have faced a decision from a (well-intentioned) tax officer, which at the very least is inaccurate. In other circumstances the decision could just be plainly wrong. One would hope that sufficient information and evidence was exchanged between the parties prior to this step but in any case, the taxpayer then has its own decision to make: accept HMRC's position or seek to challenge it (or at least ask that it be reviewed in the first instance).

Based on countless discussions with taxpayers in such circumstances, the options available at this stage are sometimes not clear to them. There is no need to commit at that point to proceeding all the way to a Tribunal hearing. One of the unique benefits of the tax tribunal system is that each party automatically is only liable for their own costs for the majority of case (or they can opt out of being liable for the other side's costs for complex matters). Therefore, if it appears that the decision made by HMRC is incorrect, there is no real downside to progressing the dispute initially and taking a decision at key stages along the way on whether to continue. This could be after receipt of HMRC's Statement of Case, after exchange of witness evidence, or even upon receipt of the skeleton argument.

In particular, it is often overlooked how important witness evidence can be in tax disputes. The theoretical or technical tax position can seem as clear as day; but often, judges are left without much evidence upon which to base a taxpayer favourable decision. It is worth keeping in the mind that for the majority of cases, the burden of proof is on the taxpayer (not HMRC). Witness evidence which is well prepared with a view to the witness being cross-examined in a Tribunal hearing can be equally useful in other settings (i.e. mediation).

Avoiding court

Mediation of tax disputes involves the parties (HMRC and the taxpayer, and their advisers where relevant) discussing the issues in hand with a view to resolving them. Mediation is an opportunity for the taxpayer/their legal representative to put forward their position and hopefully persuade HMRC that the sums claimed are not properly due, or at the very least, narrow the issues in dispute. It sounds simple on the face of it but there are various elements to keep in mind, and pitfalls to avoid.

One of the most obvious challenges to tax mediations is that the mediator (the person in the middle who tries to help the parties resolve the dispute or narrow the issues) works for HMRC. In practice, the mediation team within HMRC are excellent and keep the need to be impartial at the front of their minds. There has been a significant rise in the use of mediation of tax disputes and that is unlikely to fall, particularly given how long it can take to have a matter listed for a hearing in the First-tier Tax Tribunal.

From a timing perspective, mediation is the clear winner; HMRC aims to resolve ADR matters within 90 days of a successful ADR application. There are various deadlines along the way for both parties to commit to, which keeps the momentum up and hopefully means that the parties can meet (virtually or in person) potentially within a matter of weeks.

Unlike other forms of mediation, where the mediator brings the parties together and facilitates discussions around an acceptable settlement sum (where monetary claims are involved), it does not work in the same manner for HMRC tax mediations. HMRC officers are bound by the Litigation and Settlement Strategy. This document sets out the way in which disputes should be conducted and settled by HMRC. There are quite a few aspects to the LSS which signify how different it can be to mediation in normal civil litigation.

In other forms of mediation, the parties can generally agree to whatever amount they like when there is some form of monetary claim involved; there is no real need for it to be justified to anyone else for it to be binding on the parties. Unfortunately, HMRC are not able to 'split the difference' between the amount of tax they consider to be owed and the amount the taxpayer is offering. If HMRC consider that £100 of tax is due, they cannot 'shake hands' for £90.

Similarly, where commercial parties are involved in a dispute, it is not just the amount at stake that is factored in when it comes to considering settlement. Issues such as the time it takes for the business to dedicate to the dispute or the legal and advisory fees in respect of the same over the course of a potentially long litigation would normally be carefully balanced against the potential benefit of proceeding/settlement. HMRC cannot factor in the length of time it might take them to get through the courts in order to get to the tax they think is due. Nor can they factor in the amount of legal fees that might be incurred externally in respect of the same.

In addition, the less formal surroundings of a (virtual) mediation with HMRC can be naturally less intimidating to taxpayers than a Tribunal or court room and avoids the need for a public hearing and judgment. This is not something which should be overlooked. Indeed, for some clients, the thought of stepping foot in a courtroom and details of their case being publicly available in a judgment, even if there are no issues to consider with regards to the taxpayer's behaviour with a view to penalties, would be unfathomable. There is the additional benefit that mediations do not need to meet the various prescriptive requirements for a Tribunal hearing (for example, long bundles or weighty skeleton arguments).

Mediation is a very useful tool in the arsenal of tax advisers and it should not be reserved for the most extreme or complicated disputes. It can be incredibly helpful at unlocking disputes. In the modern world where so much is done via email, there can be months or even years of correspondence about a single issue. It is often the case that parties can be amazed at how quickly misunderstandings in the respective positions are made clear through a few hours of discussions. Meetings/calls with HMRC, can also be very helpful in moving people away from seemingly intransigent positions.

Reasons to be careful

There should be a degree of caution with HMRC mediations though.

Traditionally, mediations are 'without prejudice'. Put simply, this means that neither party could bring to the court or Tribunal's attention anything the other party said on the basis that it was view a view to try and reach settlement. The major exception to that for HMRC mediations is where there is a 'tax fact'. HMRC defines a tax fact as "a fact that has legal and technical implications for a customer's tax liability", which means it therefore is "not capable of being without prejudice". For example, this can mean situations where a taxpayer/adviser refers to the receipt/making of a supply which HMRC was not previously aware of.

It is hoped that this should not cause an issue in the vast majority of mediations; however, it is definitely something to be aware of given the scope for a potential dispute as to whether something amounts to a tax fact.

Worth a go?

The HMRC ADR unit consider applications for mediation and there is clear guidance as to which matters will or will not be suitable. It is worth having a detailed read if mediation is being considered. Although there are some justifiable concerns about the process, mediation is still an incredibly attractive option for individual or corporate clients across a range of contentious matters.

If this has the additional benefit of also removing a significant number of cases from the Tax Tribunal's process, this can only improve the efficiency of the overall tax disputes process; thus benefitting HMRC, taxpayers, and advisers alike.

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