HMRC Enquiries Investigations & Powers

February/March 2020

The power of Schedule 36

Beware the pitfalls of the information notice

Yet another IR35 defeat for the taxman

Ramifications of the RALC Consulting tribunal

The face of an accountant who is **supported** by the ICPA

We have listed some of the most common symptoms of an ICPA member below

Taxman sets up secret unit to probe IHT avoidance

HMRC has created a secret unit to investigate the use of family investment companies (FIC) by the very wealthy to avoid paying inheritance tax.

It puts family offices with a combined total of more than $1tn in assets within its sights.

The tax authority set up the team in April last year amid growing concern that the wealthy avoid paying tax through sophisticated legal loopholes and was first reported by the Financial Times.

The unit is targeting FICs, which are increasingly being used as vehicles to hold stocks and other assets. It means the tax on dividends is paid as corporation tax instead of personal income tax, which means lower rates according to lawyers.

If children are brought in as co-shareholders, then inheritance taxes can be reduced in some cases.

HMRC told the FT that the Family Investment Company team was established in April 2019 to look at FICs and do a quantitative and qualitative review into any tax risks associated with them with a focus on inheritance tax implications.

HMRC defended its position not to reveal details about the new team because doing so "would allow opportunistic individuals and would-be avoiders [to] identify where HMRC is devoting resources and arrange their activities to escape challenge".

Welcome

WELCOME to the latest edition of HMRC Enquiries, Investigations and Powers e-magazine.

We've loads of great articles in this issue, including news of yet another IR35 setback for the Revenue – see page 14 for more. Our tax guru, Mark McLaughlin asks whether some discovery assessments are really made using HMRC's best judgment (page 4); while we add balance by reporting on the taxman's various successes against those willing to circumvent the law.

Finally, this issue was published before the Chancellor's 11 March Budget – some of the issues tackled in this publication may be affected by it.

Happy reading,
The Armstrong Media team

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Plucked out of thin air?

Mark McLaughlin asks whether some discovery assessments are really made using HMRC's best judgment

HMRC's discovery powers are an important and valuable weapon in its tax compliance armory. There are separate discovery provisions for individuals and companies. This article focuses on the former (TMA 1970, s 29).

The discovery legislation broadly provides for an HMRC officer (or HMRC) to make an assessment of income tax or capital gains tax which in their opinion ought to be charged in order to make good a loss of tax brought about due to (for example) a taxpayer's omission or under-declaration of income or gains.

There are statutory safeguards to protect taxpayers against discovery assessments in certain circumstances, depending on whether the taxpayer has submitted a self-assessment return for the relevant tax year. The extent to which taxpayers are protected by these safeguards has been the subject of many disputes with HMRC, and quite extensive case law over many years.

Don't overlook the obvious

The natural instinct of taxpayers (and advisers) when discovery assessments are issued is to carefully review the safeguards (in TMA 1970, s 29(3)-(5)) to check whether the assessments have been validly made. However, the basic requirements for a discovery assessment (in s 29(1)) should not be overlooked.

First and foremost, there needs to have been a 'discovery' of an omission, under-declaration etc. by HMRC. HMRC may then "make an assessment in the amount, a further amount, which ought in his or their opinion to be charged in order to make good to the crown loss of tax".

HMRC cannot simply base its discovery on figures plucked out of thin air. In Johnson v Scott [1978] STC 48, Walton J said: "…what the Crown has to do is…on the known facts, to make reasonable inferences…the Inspector's figures…ought to be – fair. The fact that the onus is on the taxpayer to displace the assessment is not intended to give the Crown carte blanche to make wild or extravagant claims. Where an inference, of whatever nature, falls to be made, one invariably speaks of a 'fair' inference. Where, as is the case in this matter, figures have to be inferred, but has to be made is a 'fair' inference as to what such figures may have been. The figures themselves must be fair."

Onus of proof

If a discovery assessment is not based on fair and proper inferences from the facts, the assessment is open to possible challenge. On appeal against a discovery assessment, it is generally accepted that the onus is on the taxpayer to prove that the assessment is inaccurate. However, in Cussens v Revenue and Customs [2019] UKFTT 543 (TC), the First-tier Tribunal reminded HMRC that it must bear the onus of establishing that the discovery assessments were made on a reasonable basis

In Cussens, on 18 January 2018 HMRC issued discovery assessments to the taxpayer for the tax years 2004/05 to 2015/16 inclusive. The basis for the discovery assessments was that HMRC alleged they had made a discovery that the taxpayer had failed to declare trading profits for each tax year. HMRC originally began checking the taxpayer's tax position for each of the tax years on 5 April 2017 and requested details from him. The taxpayer failed to produce any significant documentation and/or narrative, and subsequently appealed the assessments, asserting that he had no income over the relevant tax years which would result in an income tax liability.

The First-tier Tribunal pointed out that the onus of establishing that the assessments were made upon fair and proper inferences drawn from established facts rested with HMRC. The tribunal also noted that the assessments were subject to a statutory review. The review conclusion letter made it perfectly clear that "best judgment" was the basis for the assessments but failed to consider what (if anything) had been taken into account in arriving at best judgment. There was nothing in the documentary evidence to suggest that any thought, consideration or analysis whatsoever was undertaken by either the HMRC assessing officer and/or the review officer to decide whether the quantum of the assessments was reasonable. The taxpayer's appeal was allowed.

What is 'best judgment'?

In Cussens, the judge noted that the discovery assessments had been subject to a statutory review, and that the review officer indicated the assessments had been based on 'best judgment'. There is no explicit reference to best judgment in the discovery legislation, so there is no statutory definition.

However, the tribunal judge pointed out that the following six principles on best judgment had emerged from case law (Van Boeckel v Customs and Excise [1981] STC 150; Rahman (No. 2) v HMRC [2003] STC 150 (albeit VAT decisions):

a. The respondents must be in possession of some material upon which a best judgement assessment can properly be based;
b. The respondents are not required to undertake the work which the taxpayer would ordinarily undertake so as to arrive at a conclusion about the exact amount of tax due;
c. The respondents are entitled to exercise their best judgement power by making a value judgement on the material available;
d. This tribunal should not treat an assessment as invalid simply because it takes a different view as to how the best judgement could or should have been applied to the material available to the respondents. Before the tribunal interferes, it needs to be satisfied that the purported best judgement assessment was wholly unreasonable;
e. The tribunal is to start by assuming that the respondents have made an honest and genuine attempt to arrive at a fair assessment.
f. It is for the tribunal to arrive at the proper sum for the tax payable in the event that it decides that the assessment(s) fail to satisfy the best judgement criteria.

Furthermore, in Homsub Ltd v Revenue and Customs [2019] UKFTT 536 (TC) the tribunal held that in addition to the factors mentioned above, any assessment said to be to best judgment will necessarily have to be methodologically sound or, at least, not methodologically flawed.

Don't be bullied

Cussens is perhaps most notable for the tribunal's severe criticism of HMRC's approach to the discovery assessments in that case.

The tribunal was firmly of the view that HMRC's use of a net profit margin of 50% of supposed turnover had been simply "plucked from the air". Furthermore, the tribunal concluded that the assessments were "so wild, extravagant and unreasonable" that they were not raised for the purpose of making good to the Crown a loss of tax and so were not authorised by TMA 1970, s 29.

HMRC had decided to issue the assessments "almost in terrorem", with a view to persuading the appellant to engage properly with HMRC in the matters under review. The net profit margin of 50% adopted by HMRC could not properly be described as 'best' judgment.

While it would generally be better to comply with HMRC information requests timeously if applicable, taxpayers and advisers should be wary of unrealistic assessments by HMRC to frighten or provoke taxpayers into responding to requests for information where there are delays in providing it for some reason.

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HMRC opens 300,762 self assessment investigations

HMRC opened 300,762 investigations into self assessment tax returns, according to data released in 2019 for tax year 2016/17. The tax authority collected £1.2bn in extra tax from investigations into self-assessment tax returns in 2018/19.

Analysis by accountants Moore (formerly Moore Stephens) shows the level of risk, warning taxpayers to be careful when filing tax returns as mistakes, although often not deliberate, act as a red flag for HMRC, which can lead to investigations and even penalties.

Filing returns late can also attract HMRC's attention. A total of 477,000 tax returns failed to meet the deadline last year, leading to £47.7m of penalties being imposed.

The size of a penalty imposed through a tax investigation depends on whether HMRC believes the mistake was made deliberately or not.

The penalty for a 'deliberate' mistake can be as much as 100% of the amount of tax in question whereas the penalty for 'failure to take reasonable care' is 30%.

HMRC imposed over 31,500 penalties for deliberate behaviour during the 2018/19 tax year.

HMRC's methods of data collection are becoming more advanced and are more invasive than some countries.

For example, tax authorities in France have only just been granted permission to scan social media accounts of taxpayers to gather evidence during investigations – something HMRC has been doing for years.

Bridget Culverwell, director at Moore, said: "HMRC will be combing through tax returns looking for reasons to investigate you – so it's crucial you don't make basic mistakes.

"Tax investigations can be very stressful and even a basic investigation can drag on for months.

"If there are sudden increases in your costs or reductions in your income, that reduces your tax, then make sure you explain these to HMRC when you submit your return. That may help stop an inquiry being opened."

Rembrandts donated to settle inheritance tax bill

Six etchings by Dutch master Rembrandt have been given to the Ulster Museum in Belfast as a result of a deal over an outstanding tax bill, the first works by the artist to be acquired by a Northern Ireland museum.

The works were given to Arts Council England under the acceptance in lieu scheme, which allows taxpayers to transfer important works of art and heritage objects into public ownership while paying inheritance tax (IHT). They formed part of an agreement to settle an IHT bill of over £150,000.

Ulster Museum has already put two of the etching it has received as a result of the tax settlement on display in its current exhibition dedicated to landscape painting. These are Six's Bridge and The Adoration of the Shepherds.

The etchings date from the 1630s to the 1650s. The other four works – Bearded Man in a Furred Cap and Robe; The Artist's Mother; The Sleeping Herdsman; and The Descent from the Cross by Torchlight – are four due to be exhibited at the venue soon as part of a planned exhibition on Rembrandt.

Kathryn Thomson, chief executive of National Museums NI, said: "This gift immeasurably transforms the Ulster Museum collection, as these are the first works by Rembrandt to enter a public collection in Northern Ireland.

"We are very grateful to Arts Council England for this allocation from the acceptance in lieu scheme. We are so excited for the opportunity for our visitors, from here and further afield, to see the work of one of the world's most celebrated artists in Belfast."

HMRC probes into small firms raise £4.9bn

HMRC collected £4.9bn in extra tax from investigations into individuals and small businesses in 2018-19, but only had to spend £309m on staff to achieve that. This extra tax included £1.2bn from investigations into underpaid income tax.

HMRC's individuals and small business compliance (ISBC) directorate oversees the tax compliance of individuals and small businesses, which it classes as any company with fewer than 20 employees and an annual turnover below £10m.

According to analysis by Pinsent Masons, while HMRC's focus is primarily on large companies, the high level of returns it has received from investigations at the other end of

the spectrum means it may consider investing more into staff targeting this taxpayer group.

The law firm's figures show HMRC raises £16 for every £1 it spends on staff carrying out investigations into the tax affairs of individuals and small businesses,

Steven Porter, partner at Pinsent Masons, said: "For HMRC, this is an outstanding result. These returns will spur HMRC on to do more – taxpayers can therefore expect more attention and more investigations.

"Individuals and small businesses are more vulnerable to tax investigations as they are less likely to have access to advisers who can shut HMRC down."

Pinsent Masons said that a key area of focus for HMRC when targeting individuals is self assessment tax returns. If HMRC identifies a mistake on a tax return, then it may conduct an audit of returns filed in previous years too, increasing the likelihood that it will find further mistakes.

Wolves in sheep clothing?

Russell Cockburn looks back on the days when Cumbria's sheep farmers tried to, er, pull the wool over his eyes...

A week or so ago I attended a parish council annual dinner in the village next to ours (just as a hanger on, my wife is involved in local politics). Anyway, it was an excuse for a good night out!

During the meal I chatted to the farmer sitting next to me whose flock of Herdwicks had started lambing the night before, so he was looking a bit tired and was expecting to be up most nights for the next few weeks or so as he has 1,300 ewes ready to lamb. At times like those I am reminded how pleasant it is to work in a comfortable office even during the hectic January tax season!

This afternoon I had occasion to think about this chap again when, glancing out of my window just after lunch (I often work from home), I beheld a dozen or so sheep who had escaped the field opposite and were happily munching away on the new growing snowdrops in the verge. A quick post on the village Facebook page soon alerted him to the problem and he turned up in his Land Rover to shepherd them back into the field.

Lambing starts early here in West Cumbria compared with many other parts of the north of England (late January) and this feature of the local farming economy reminded me of some of the more interesting discussions I had as a trainee tax inspector (many years ago) with farmers and their tax advisers/accountants about stock valuations – a couple of which I thought I might share with you.

Wet behind the ears

Most of the farmers I dealt with in those days clearly thought I was a little wet behind the ears (I was), and that they could pull the wool over my eyes (they could and frequently did), to the extent that they would so confuse me with their tales (they usually did) that they would sometimes end up paying less tax than they started out owing. I know, I don't think I was a very good tax investigator.

My first tax enquiry on a sheep farm involved an argument about 'lambs at foot' for a farmer whose flock also started lambing in late January and who, for some unusual reason that I never really understood, had a February 28th year end for his annual accounting period. My boss had handed me the case and said that he through there was something missing from the stock valuation included in the accounts for the ewe flock as it showed hardly any lambs at foot, although the lambing period had probably started in mid to late January. On further investigation the farmer admitted that his flock had begun lambing that year on the third week in January and that by the end of February he would have had at least 800 little darlings gambolling around his lower fields in their little plastic jackets. What he was not willing to agree was that they should be included in his stock valuation as in his view they had no value at the year-end only a few weeks after they were born.

HMRC does not agree with this viewpoint and never has done. I had to politely explain to him that the department's view was and is to this day that some value must be attributed to these very young animals even if it was to be a purely nominal amount.

HMRC's view is that the valuation of immature and 'unweaned' animals should normally be calculated using their long accepted 'deemed cost' method if actual costs cannot be identified (which is not normally easy). This method is based on the open market value of animals of a similar age and type and is acceptable to HMRC generally where farm animals are treated as stock in trade. In these cases it is then acceptable to base the 'deemed cost' on a 75% of market value for sheep and HMRC also accepts that it can be appropriate to value mother and young together because that is what at that stage would be regarded as 'the market unit'. Now while the value of such very young animals may be small it nevertheless has to be included, and I often had lengthy discussions with farmers about these matters.

The only situation where the above method of stock valuation is not appropriate is where the lambing mother is part of a farm flock that is dealt with on the 'herd basis'. On this method mature animals are treated as in effect a fixed asset rather than as stock in trade for tax purposes. Where this is the case HMRC takes the view that even where there is no market or a very limited market in for unweaned lambs at foot it is still not acceptable to leave such animals out of the annual year end stock valuation. If this is the case then a cost basis is usually acceptable to HMRC and these costs, which in such cases must normally be identified as the costs of production should be included as the year end valuation and then should be carried forward to be set against the eventual sale price.

Thorny valuation issue

Commonly, when I raised this somewhat thorny valuation issue with most sheep farmers they tended to look at me as though I had just crawled through one of their ubiquitous hawthorn hedges or from under the nearest rock and then subjected me to a tirade of gentle abuse, usually littered with anecdotes about having to chase lambs all over their fields just in order to count them for their accountant at the year-end. So no wonder it was difficult to be accurate about how many they actually had. This latter point was of course nonsense; farmers, in my experience, know exactly how many lambs their flock has produced, it's their livelihood after all and they spend hours of hard labour bringing them into this world, usually in the depths of freezing winter nights. They are going to make very sure they count them properly and look after them as best they can.

Lower of cost and net realisable value has long been established as the general principle for accounting and tax purposes where such stock valuations are concerned, but there is no doubt this is not an easy subject and remains controversial to this day, when it can clearly be argued that there is in fact no normal market at all for such young animals. Indeed, many listeners to our local Radio Cumbria about this time of year will be aware they offer a 'lamb bank' service, by which lambs that have been rejected by their mothers or are surplus to requirements can literally be 'farmed out' to other farmers who have ewes which have lost their progeny for some reason.

Many farmers quoted this to me as clear evidence that lambs that were only a few weeks old have no real value and no market existed for them, and I usually found myself agreeing with them and accepting purely nominal values for such young stock just to settle the matter. However, where the mature flock is, say, 2,000 breeding ewes even this can result in a significant uplift in the year end stock value and a resulting settlement that met with the approval of my boss in the tax office. Happy days!

Gone with the wind

The other interesting excuse I remember was the farmer whose stock was clearly much lower than it should be at his February year end – which he put down to wind! Not the gastric variety but a great storm which literally blew about 50 or so poor little lambs off the fellside in the course of one dreadful night.

As a trainee inspector at the time my boss was sitting in on the meeting and raised his eyebrows well past the level of the ceiling at this unexpected explanation. He immediately left the room and returned after a few minutes with a map of the local area and three files for the farmers whose land surrounded the taxpayer under investigation. He then said he had checked the prevailing wind on the night of the storm with the Met Office and proposed to check the stock of the other farms in the downwind direction, to see if they had had an unexpected increase in lambs at foot. Needless to say, this bullish approach met first with incredulity from the farmer and then a realisation that perhaps we were not quite so naive about farming matters as he expected.

When a farmer suffers a sudden loss of stock, for whatever reason, it is also common to see an increase in their vet's bills at around the same time, if illness or some unexplained deaths have occurred. Farmers rarely let such matters go unchecked so the absence of such extra expenses also casts doubt on the veracity of their often amusing and sometimes incredible justifications. That not to say that such reasons for shortfalls cannot be genuine at times, they often are, but needless to say the inventiveness and imagination of such , 'customers' always gave me cause for amusement and frequently brightened up the life of what could sometimes be a rather tedious civil service day.

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The power of Schedule 36

Beware the pitfalls of an Information Notice, warns Salman Anwar

HMRC has numerous powers to conduct enquiries or make assessments, but the reality is that HMRC requires evidence to come to their conclusions and that evidence comes in the shape of documents and information. The powers contained in Schedule 36 of the Finance Act 2008 are HMRC's primary weapon for evidence gathering. HMRC can demand the evidence from the taxpayer (through a taxpayer notice) or from a third party (through a third party notice), together referred to as 'information notices', but there are strict limitations on what they can demand.

Unfortunately, experience suggests that HMRC often operates on the basis that if you don't ask you don't get, with the result that they may sometimes ask for more than they are entitled to.

If you know the rules you may be able to limit their requests quite substantially – curtailing the length of an enquiry as well as potential costs.

First principles

HMRC can seek documents and information that are in the power and possession of the taxpayer (or a third party) that are reasonably required for the purposes of checking the tax position of a taxpayer. There are many distinct concepts in this statement that we will consider in turn.

What's the difference between documents and information? A document exists but information can be brought into existence. Both can be statutory records (covered later). The definition of documents extends to anything in electronic format and could, for example, include your accounting package.

Possession and power: This is relatively straightforward. Possession means you already have it and power is the ability to obtain it. Your client's historic bank statements may not be in their possession, but it would be in their power to request these from the bank (whether they have retained them is another matter!).

Reasonably required: This can be quite a broad and subjective concept, but the key thing to bear in mind is that the test is for the document or information to be reasonably required for the purposes of checking the taxpayer's tax position. From experience the definition of what HMRC considers to be reasonably required can differ from officer to officer – and may differ from what the Tax Tribunal thinks.

Tax position: Includes past, present and future tax position with regards to most major taxes or duties HMRC has responsibility for – but it is worth bearing in mind that there are separate powers for Customs duties as well as National Minimum/Living Wage. Theoretically, HMRC could ask for details of a transaction before it has completed, although you might be able to challenge the relevance to tax position if you haven't submitted a Return yet. This is an untested area.

Limitations on HMRC

Open enquiry or reasonable suspicion: Where HMRC has an open enquiry the criteria it needs to fulfil to issue an Information Notice are those noted above. However, where it is checking a year that is outside the scope of the statutory enquiry (under S9A or Para 18, for example) then an officer of HMRC needs to demonstrate that they have reason to suspect that there has been an omission/underassessment of some sorts in that period. This is a vague concept but bear in mind that HMRC needs to demonstrate careless or deliberate behaviour (where a return has been submitted) in order to be able to make assessments relating to tax years which fall outside the normal assessment time limits. However, the bar to issuing an Information Notice is only set at reason to suspect.

Old documents: For documents created more than six years ago, at the point the notice is issued, the agreement of an authorising officer is required.

Legal or litigation privilege: HMRC cannot ask for information relating to the conduct of an appeal, Journalistic material or personal records (as defined in section 12 of POCA 1984) (para 19 of Schedule 36). Similarly, any requests for information of documents that are covered by Legal Professional Privilege (includes Advice and Litigation Privileges) cannot be required by an information notice (para 23 Schedule 36). It is worth bearing in mind that these privileges do not apply to an accountant's legal advice, lawyers must be involved.

Limitation on appeals

Statutory records: The taxpayer has no right of appeal if the documents or information requested is part of a taxpayer's statutory records. While there is no precise definition of what constitutes a person's statutory records, the Taxes Acts define these as the records required to prepare and complete a correct return for a particular year. The Taxes Acts also set out the time limits for keeping such records and if the time limits have lapsed then they are no longer statutory records.

There is also a view that there is a potential to argue that a particular statutory record might not be reasonably required for the purposes of checking a particular aspect of a tax return – so that, for example, the Inspector might not be able to ask for your sales invoices if he is questioning the amount of bank interest you received – although this remains to be tested.

Tribunal approved notice: The taxpayer cannot appeal a notice that has had prior approval from a Tribunal. The only avenue for challenge would be by way of Judicial Review of the Tribunal's decision to approve a notice.

Biggest pitfalls by HMRC

The single biggest category of error we see from HMRC is poor wording of the requests within a notice. Tax cases have concluded that, because a failure to comply with a notice can result in a penalty, it is imperative that the wording must be crystal clear and unambiguous. Note this quote from Graham Pitcher v HMRC [2017] UKFTT 406: "When a penalty imposed by the state is under consideration, it is axiomatic that a penalty can only be imposed if it is clear to the citizen exactly what he has to do to avoid the penalty. This is an embodiment of the principle of legal certainty" [emphasis added]

Any notice that uses jargon, short hand or unclear terminology is ripe for challenge and will likely be invalid for the want of clarity. Even the inclusion of one 'etc' can ruin a notice. As an example a request for 'VAT Bad Debt Ledger for the QE 3/18' would likely be too vague and invalid.

Another error made by HMRC is asking for information and documents for a period outside the enquiry period without meeting the above tests.

Biggest pitfall by taxpayers

Failing to appeal the Notice: Not appealing a notice at the outset can severely limit your chances of a successful appeal against a subsequent or later penalty. The leading authority on this subject is the decision in the PML Accounting Ltd, R (On the Application Of) v Revenue and Customs [2018] Civ 2231. To analyse this would require an entire article on its own but the key point is to lodge an appeal if you remotely believe there to be inadequacies in the Notice.

Sending in too much: Do not send in more than is required by the notice. For example, if the request is for bank interest details then supply a certificate of bank interest paid – not your statements for the entire year. Likely consequences may be a lengthy enquiry into all your deposits or withdrawals (to the extent where we have seen a taxpayer having to 'prove' that a regular payment to a family member was not the undisclosed employment of a worker that should have been subjected to PAYE!).

Lastly, HMRC has the power to visit premises, which are similar in nature of the information powers, but that would require a separate article to explain.

Conclusion

Schedule 36 is the biggest weapon in HMRC's armoury. If you know the rules, you might be able to spike their guns and, while that might not end the battle it might put the opposing forces on a more even footing.

- ***Salman Anwar**, Senior Manager – Tax Investigations, Mazars LLP*

Penalty for incorrect zero rating certificate

FTT decision raises a number of serious issues and highlights how complex VAT has become, says Les Howard

Westow Cricket Club had a new pavilion constructed. It issued a zero rating certificate to the building contractor on the basis that the building was to be used as a 'village hall,' as defined in Note 6(b) to Sch 8, Group 5.

The certificate was invalid since the club was a Community Amateur Sports Club (CASC). It is now well established that a CASC is NOT a charity. It is therefore unable to benefit from zero-rating under the 'Relevant Charitable Purpose' provision.

HMRC issued a penalty assessment on the grounds that the club had issued an incorrect certificate. The club argued that it had a 'reasonable excuse.' Perhaps surprisingly, the FTT found against the club.

I do disagree with the conclusion of the Tribunal on this occasion! Here are my reasons:

1. The FTT quoted HMRC Notice 708, para 14.7.4, without qualification. The wording of this paragraph is now incorrect, following the Upper Tier decision in Caithness Rugby Football Club.

2. HMRC's ruling commented that their policy was that they would not provide a definitive response where the point is clearly covered by published guidance. Evidently the matter was not clear; why would the club write if it were clear!?

3. The HMRC officer did give an indication that the club would be entitled to issue a zero-rated certificate.

4. Upon receipt of the HMRC letter, the Club Treasurer did read the relevant part of Notice 708. He concluded that the certificate was validly issued and signed it on behalf of the club.

5. it was a further three years later that HMRC checked whether the certificate had been properly issued.

6. Para 4 of the decision refers to "a certificate for zero rated and reduced rated building work." Another deficiency missed! No reduced rate applies for RCP construction work!

7. The club's appeal was that they had followed HMRC's guidance. This created a 'legitimate expectation,' which ought to provide a reasonable excuse.

8. The FTT concluded that, viewed objectively, the facts could not constitute a reasonable excuse. It provides two 'strands of reasoning,' explained in paras 21-25 of the decision.

My view is that the FTT has appeared to have missed the point. It failed to consider how the club responded to its communications with HMRC. The club officer read the HMRC letter, and then the published guidance referred to, issuing a certificate in the form set down in the Notice. There can be no criticism of the club for not being aware of the deficiencies in HMRC guidance, especially as the FTT missed it too.

The FTT has applied a 'was the club right or wrong?' test here. This is quite different to the reasonable excuse test. It quoted Perrin which is a leading case, but seems not to have applied its reasoning correctly.

Arguably, the club should have read the correspondence and guidance more carefully (that is easy to say as an adviser). Also, the club should have sought technical VAT advice (also easy to say as an adviser).

FTT decisions are persuasive, not binding. Subsequent decisions may choose to depart from this one.

One further comment. HMRC seem to have become more aggressive of late. I would therefore expect more penalties to be issued for incorrect zero-rate certificates.

Check out the decision here: https://tinyurl.com/r79tn69

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New report on signing documents electronically

The Law Commission has published a new report about the use and validity of electronic signatures on documents, Ross Martin has reported.

The company, which supplies tax resources to accountants, said the report is the result of a law reform project started in 2018 to address uncertainty to the formalities around the electronic execution of documents. It was especially looking at documents and deeds where there is a statutory requirement that they must be 'signed' and have requirements of witnessing and delivery.

The report does not apply to wills, which are the subject of another Law Commission project. Registered dispositions under the Land Registration Act 2002 are specifically excluded.

The conclusion of the report is that an electronic signature is capable in law of being used to execute a document (including a deed) provided that:

- the person signing the document intends to authenticate the document, and
- any formalities relating to the execution of that document, (such as that the signature be witnessed or be in a specified form e.g. handwritten) are satisfied.

- An electronic signature is admissible in evidence in legal proceedings, for example, to prove or disprove the identity of a signatory and/or their intention to authenticate the document.
- Unless the relevant legislation, contractual arrangements, or case law specific to the document provide otherwise, common law adopts a pragmatic approach and does not prescribe a particular form or type of signature.
- The Courts have held the following non-electronic forms amount to valid signatures and the law commission says that electronic equivalents are also likely to be recognised by a court as legally valid:
  - signing with an 'X' or a mark, even where the party executing the mark can write.
  - signing with initials only.
  - using a stamp of a handwritten signature or printing of a name.
  - a description of the signatory if sufficiently clear, such as 'Your loving mother'.
  - For a deed to be valid it must be signed in the physical presence of a witness who attests the signature, even where both the person executing the deed and the witness are using an electronic signature.

The report also considers other issues to using electronic signatures, such as security. It advises that three key questions should be considered for any document, whether signed electronically or in wet ink. Users of electronic signatures should satisfy themselves that their process for dealing with signatures will provide sufficient evidence of the answers to the questions, especially if there is any dispute about the transaction.

- How can you be confident that person 'A' signed the document, and not another person pretending to be person 'A'?
- Does person 'A' have the capacity, and the requisite authority to sign the document, either for themselves or for their principal, usually a body corporate?
- What document is being signed?

The report contains some more specific guidance about signatures provided by particular bodies such as Companies House, the Land Registry and the Intellectual Property Office.

The Office of the Public Guardian has, however, confirmed to the Law Commission that they currently will not accept electronic signatures for lasting powers of attorney and have no plans to change this.

Late-paying taxpayers landed with £816m in fines

HMRC raised £816m in fines in 2018-19, up from £620m in 2015-16, an increase of 32% according to data obtained by Price Bailey.

This is a much faster rate of increase than the amount of tax collected by HMRC, which has increased by 19.2% from £495bn to £590bn over the same period.

Price Bailey says the amount of data on taxpayers at HMRC's disposal, and its ability to analyse that data, has significantly increased in recent years, largely as a result of improvements to its Connect software system, which now has enhanced capability and wider access to data sources.

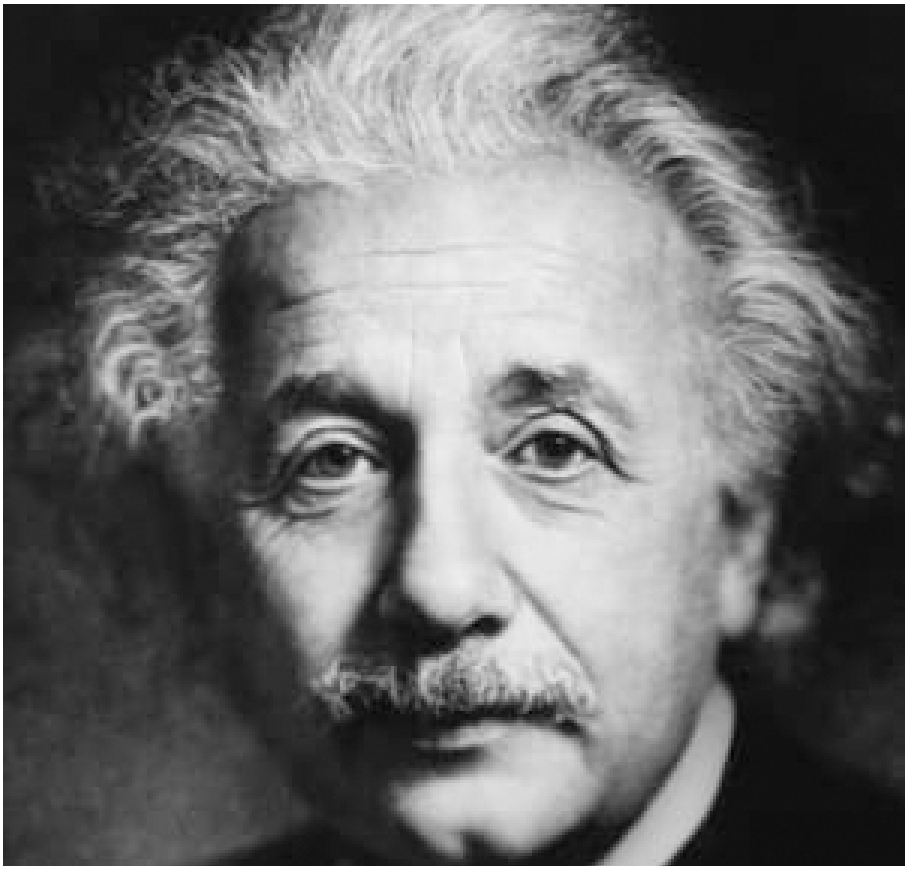
Jay Sanghrajka, tax partner at Price Bailey, said: "The amount issued in fines is increasing at a much faster rate than the amount collected in tax, which means that HMRC is fining a higher proportion of taxpayers and using new powers to impose substantially heavier penalties.

"The amount of data HMRC collects and cross-references allows it to form a more complete understanding of taxpayers' liabilities. This means that HMRC can challenge a greater number of taxpayers at a significantly lower cost.

"Discrepancies now come to light much sooner. Its software can automatically check information reported in tax returns against bank accounts and make sure they tally. Previously, checks of this kind would have been time-consuming but HMRC's software can spot any inconsistencies swiftly and flag those for further investigation."

Will sanity ever return to HMRC?

Andy Vessey digests the ramifications of the RALC Consulting Ltd tribunal – yet another IR35 failure for the taxman



The definition of insanity is doing the same thing over and over again and expecting different results. When it comes to IR35 that seems to be HMRC's policy because they don't appear to heed any lessons from history and all the time they are wasting taxpayers' money pursuing IR35 cases up a blind alley. The latest case to join the Revenue's catalogue of cock-up's is RALC Consulting Ltd.

A few years ago I represented Ian Wells of Jensal Software Ltd in a case that should never have gone to tribunal. RALC is another of those cases but the similarity does not end there. One of RALC's end client's was the Department for Work and Pensions (DWP) and, rather than using their own legal team, HMRC instructed legal counsel from Deveraux Chambers in London to make the best of a bad job; just like Jensal.

Enquiry period

HMRC focused on the period 6 April 2010 – 5 April 2015, during which time Richard Alcock, IT contractor and director of RALC, had contracted to Accenture (UK) Ltd and the DWP.

In March 2017, HMRC raised tax and NIC assessments for all years totalling over £243K. Although the department had also issued an NIC Decision for 2010/11 for £7,658, they had to forego this as it was statute time barred. What about the tax assessment for that year and 2011/12? Was that not out of time too? Not according to HMRC, as they argued that Alcock had acted carelessly in carrying out the requisite IR35 due diligence and therefore they were justified in extending the time limits.

In 2008, Alcock's accountants reviewed a contract to provide services to DWP via Parity Resources and advised this fell outside of IR35. As the terms of RALC's contract with Accenture were similar to that of the Parity contract, Alcock reasoned that this too was not caught by IR35. HMRC said this was not good enough and he should have sought specific and separate professional advice for that contract.

RALC worked on the following contracts during the enquiry period:

The first two Accenture contracts were working on DWP programmes, with the final contract involving a Police Scotland Programme.

Is that all you've got?

In addition to Alcock's own evidence, he was supported by seven other witnesses, three of whom were from Accenture and two from DWP. A pre-hearing had rejected a witness statement of Dave Chaplin of Contractor Calculator fame, as it contained both opinions and non-expert evidence about IR35. Neither would the Tribunal accept Chaplin's CEST tests purporting to be independent testing of RALC's arrangements.

In contrast, HMRC relied on the notes of a telephone conversation held in January 2016 between themselves and a former DWP deputy director to whom Alcock had briefly reported to during one of the contracts. Despite three requests the notes were never signed by the deputy director. In the judge's opinion this reduced the evidence to hearsay, "filtered through the medium of an HMRC note taker".

Period	End client	Role
08.10.10 – 20.07.12	Accenture	System Delivery Integration Manager/Client-side Delivery Assurance Lead
22.10.12 – 28.04.13	Accenture	Agile Delivery Factory Manager
04.03.13 – 07.12.13	DWP	Senior Suppliers Manager
16.12.13 – 14.02.15	Accenture	Design Consultant

IR35 did not apply because...

Mutuality of obligation (MOO): Alcock had been an employee of Accenture from September 1998 until March 2008, when he left to provide his services through RALC. During his time at Accenture, he had worked on DWP engagements, as DWP had been a client of Accenture. In May 2008, RALC's first contract was with DWP.

HMRC sought to argue that Alcock's long history of working as an employee for Accenture and the operation of the contract in practice led to an expectation that Alcock would be provided with work by Accenture every business day during the course of an assignment, unless agreed otherwise, such that it crystallised into a legal obligation. The Tribunal rejected this notion because there was no binding expectation, guarantee or accepted contractual right for RALC to be offered a minimum of work during the course of the contract as all parties realised the contract could be cancelled at any time if DWP decided to stop or abandon the project. The second Accenture contract was actually terminated in January 2013, some three months early.

The Tribunal considered that whilst Alcock provided his services for payment, the lack or insufficiency of MOO confirmed that the contracts were of a self-employed nature. DWP and Accenture paid RALC a daily rate for work done, at the agreed rate upon invoice but there was no contractual obligation beyond that. This was no more than an expectation as to the days and hours that would be worked each week and did not form any obligation. RALC would only be paid for work done, with no guaranteed obligation on the part of the end clients to provide RALC with any work during the contracts.

DWP could terminate their contract without any notice and Accenture by giving 30-days' notice and without giving a reason for such. There would be no paid notice and RALC would have no right to any fee for work done outside of the cancellation of the contract.

Control: There was no significant control over what work RALC performed nor how it was executed provided RALC delivered the final outcome in conjunction with the end client teams. Alcock was to collaborate with the end clients to agree the best way in which to deliver those parts of the project for which he or his team was responsible.

A number of other lesser factors supported self-employment, but the right of substitution was fettered by the end clients far reaching right of veto.

Carelessness

As the Tribunal upheld RALC's appeal it was not necessary for them to consider this issue.

The department really should be more selective in which IR35 fight it picks. They had opportunity to back away from this case but their pride came before their fall.

- ***Andy Vessey** is Head of Tax at Larsen Howie*

Here's an update on recent HMRC successful investigations and prosecutions

Nine jailed for running UK's largest illegal tobacco factory

The masterminds behind a £10 million fraud have been jailed after they were caught running the UK's largest illegal tobacco factory, which could produce 140 packs of cigarettes a minute.

John Watson Snr, 47, who was a director of Doncaster Greyhound stadium, Terence Jacques, 60, and security guard Russell Haywood, 48, led a 12-man gang that made millions of counterfeit cigarettes which were distributed across the North of England.

HMRC carried out coordinated raids at properties linked to the gang in County Durham and South Yorkshire in November 2015.

Officers discovered the largest tobacco factory ever encountered by HMRC inside a farm unit in Crook, County Durham. The factory had more than 24 tonnes of tobacco inside, along with 500,000 cigarettes, old imperial tobacco machinery and products used to make the cigarettes. Officers also discovered caravans that were being used by the

factory workforce.

The cigarettes produced at the factory were moved to a nearby garden centre, before being distributed to locations in the North East and South Yorkshire.

Watson Snr said he earned less than £15,000 a year at the time, but investigators discovered he had spent more than £180,000 on luxury cars and a holiday.

On 25 February 2020, 10 members of the gang were sentenced at Sheffield Crown Court.

Aleksandras Seremetjevas, 35, and Mindaugus Aleksandravicius, 47, will be sentenced at the same court on 2 April 2020.

Eden Noblett, Assistant Director, Fraud Investigation Service, HMRC, said: "This was a highly sophisticated and well organised illegal operation, which put millions of counterfeit cigarettes on the streets of the UK.

"The illegal tobacco factory was the largest HMRC has ever found, and was capable of producing commercial quantities of cigarettes. The weight of the tobacco found at the factory was equivalent to two London double decker buses."

Seven of the men admitted excise fraud at separate hearings at Leeds and Sheffield Crown Court in 2019.

The remaining five men were found guilty of excise fraud on 10 and 11 February 2020 following a trial at Sheffield Crown Court.

In total, HMRC seized cigarettes, tobacco and associated paraphernalia capable of evading more than £10 million in duty. Proceedings are under way to recover the unpaid duty.

Watson Snr and his right-hand man, Jacques, were responsible for setting up and running the tobacco factory, while Haywood managed distribution of the cigarettes across the North of England.

Seremetjevas and Aleksandravicius oversaw the day-to-day running of the factory, recruited factory workers and arranged movement of cigarettes to a unit at the Stanley Garden Centre, in Crook.

Edward Kennyford, 72, was in charge of moving cigarettes out of the garden centre. He met with drivers Christopher Wallace, 40, and Steven Quigley, 53, at a layby off the A68 in Durham to handover vans filled with the counterfeit goods. Watson Jnr, 26, helped load cigarettes into the vans at the garden centre.

Whilst the illegal activity took place the owner of the garden centre, John Seaman, 66, switched off the CCTV cameras. The drivers delivered the cigarettes to locations across the North East and Yorkshire as instructed by Haywood.

HMRC shut down the illegal factory in November 2015 when officers executed search warrants at the farm unit, garden centre, and home addresses of Watson Snr and Jacques.

Watson Snr fled the scene in his car when officers arrived at his home, but later attended Doncaster police station.

Investigations revealed he had spent more than £180,000 on cars and a holiday for 18 people. At the time he was earning less than £15,000 a year as a director at Doncaster Greyhound stadium.

Jacques was arrested at his home and a search of the property uncovered a bag containing £46,500 cash in his bedside drawer. Fingerprints found on the bag belonged to Watson Snr.

Officers also visited a unit rented by Jacques on Tow Law Industrial Estate, County Durham, and uncovered cigarette paraphernalia which could produce goods worth more than £9,000,000 in duty.

Aleksandravicius and Watson Jnr fled Stanley Garden Centre when HMRC officers arrived, but they were subsequently arrested by police nearby.

Kennyford and Quigley were arrested at a layby near Crook Community Leisure Centre with a van containing 768,000 cigarettes.

A further 256,000 cigarettes were found in Kennyford's vehicle which was parked at the garden centre.

One month later, Paul Drummond, 49, and Ryan Lowe, 40, were seen transferring cigarettes worth £96,326 in unpaid duty between two vans outside a storage facility in Barnsley.

Drummond then met with Haywood on a nearby street and exchanged a package containing £20,000 through their vehicle windows. Both men were arrested at the scene.

Duo jailed over property tax fraud

A pair of fraudsters who bought and sold over 50 properties but failed to pay nearly £1 million in tax, have been jailed for more than eight years.

Madhu Bhajanehatti, 45, of London and Himat Chana, 59, of Ilford, Essex, sold dozens of properties over an eight-year period, and evaded £991,000 in Capital Gains Tax.

Although the men disclosed some income on their Self-Assessment tax returns, they deliberately hid the sales of properties across London and Essex, an HMRC investigation revealed.

Richard Wilkinson, Assistant Director, Fraud Investigation Service, HMRC, said: "The duo believed they were above the law and showed a blatant disregard to their obligations by failing to declare substantial income from property sales."

HMRC officers discovered the men had built up their property portfolios by using the proceeds of previous sales. This was uncovered by a property taskforce set up to tackle fraud in the industry.

Bhajanehatti evaded £650,000 in tax and Chana evaded £341,000. He admitted the fraud during a hearing at Southwark Crown Court in June 2019. Chana was convicted after trial in August 2019.

The men were sentenced to a combined total of eight years and six months in jail at the same court in January: Bhajanehatti was sentenced to 50 months in jail; Chana to 52 months in jail.

Bhajanehatti was also ordered to pay back £190,086.42 in a confiscation order. He has less than three months to pay it back or he faces a further two years and six months in jail.

Confiscation proceedings for Chana are on-going. If further assets are identified in the future for Bhajanehatti, they could also be confiscated.

Payback time for tax fraudsters

Five tax fraudsters who were part of a crime group involved in one of the UK's biggest tax frauds have been ordered to repay £20 million, or face more time behind bars and still owe the money.

Michael Richards, 57 and Jonathan Anwyl, 46, both of East Sussex, Dubai-based Robert Gold, 51, Rodney Whiston-Dew, 68, of Greenwich, London and Evdoros Chrysanthos Demetriou, 80, from Oxford, were all jailed for more than 43 years. An investigation by HMRC found the group had devised a fake eco-investment scheme as a tax break for wealthy investors.

At the Old Bailey in October and Southwark Crown Court in December 2019, they were ordered to pay a combined total of £20 million or serve a further 39 years in prison. If further assets are identified in the future for any of the convicted men, they could also be confiscated.

The five men were sentenced in November 2017, to a total of 43-and-a-half years in jail, after HMRC investigators found they lured wealthy individuals to invest in Carbon Emission Reduction Certificates, which help countries hit environmental emissions targets set by the United Nations. But in reality, the money was diverted to purchase properties in the UK and Dubai, none of which was declared to HMRC. The £107.9 million fraud was one of the UK's biggest tax crimes

Gold may need to sell a property in Dubai to settle his £2.6 million bill, and Anwyl, of Ringmer, East Sussex, cashed in his pension fund to help pay off his £250,000 order. Anwyl has paid his order and Gold has until late January 2020 to pay up or face an extra jail term.

Richards and Whiston-Dew have properties in West Sussex and South-West London which they may need to sell to pay off their respective £9.9 million and £3 million orders.

Another member of the crime group, Malcolm Gold, 75, previously of Hertfordshire was sentenced to 20 months in prison in January 2017. He was subject to a confiscation order in October 2017 for £4,711, which was the amount of assets he had available at the time. The order was paid on 27 October 2017.

Print firm fraudsters stole millions from taxpayers

Five company directors from Essex have been sentenced for their part in a £3.1m fraud that saw each of them pocket hundreds of thousands of pounds of taxpayer cash.

Stephen Knight, 67, John Knight, 74, Brian Thomas, 70, Paul Murphy, 57, and Philip Sach, 53, all played a part in a complex eight-year fraud that was uncovered following an investigation by HMRC.

The five were all directors of collapsed Basildon-based large printing business Anton Group Ltd.

Some of the directors conspired to keep cash sales of waste paper 'off record', while they all shared the proceeds, cheating the public purse out of £3.1m in corporation tax, income tax, VAT and national insurance contributions (NIC).

During the fraud, the directors slashed staff pay – including their own – telling employees that this would assist with cash flow and keep the business afloat. However, while it appeared they had each forfeited £5,000 of their own pay per month, the Knights, Thomas, Murphy and Sach were covertly stealing huge amounts of taxpayer money to line their own pockets.

Alongside non-taxed off record payments, the five received significant payments from the Anton Group Ltd, separate from any legitimate forms of payment.

Initial investigations focused on suspected evasion of corporation tax due on profits from sales of waste paper bi-product to a local recycling company.

HMRC officers were told that the paper was given to the recycling company free of charge, in exchange for the installation and upkeep of machinery. But investigators found that money did change hands and the Anton Group Ltd received cash payments for the waste paper.

These cash payments were controlled by chief executive officer John Knight and production director Stephen Knight, who facilitated regular 'off record' payments to directors and employees between April 2004 and November 2012.

Around 90 fake invoices, amounting to approximately £1.4m, were also discovered in the company's accounts. These had been declared as payments to suppliers, but the funds were siphoned off into the directors' personal bank accounts and used to repay directors' loans owed to the company.

The group were sentenced for their roles in the fraud at Southwark Crown Court in January:

- John Knight: Three years in prison. Disqualified as a director for seven years.
- Stephen Knight: 28 months in prison. Disqualified as a director for five years.
- Brian Thomas: 28 months in prison. Disqualified as a director for four years.
- Paul Murphy: Two years in prison, suspended for two years. Disqualified as a director for three years.
- Phillip Sach: Ten months in prison, suspended for 12 months.

HMRC is pursuing confiscation action to recover the stolen money.

Jail for trio caught with 10 million illegal cigarettes

Three men have been jailed for a total of 10 years and nine months after they were caught with millions of illegal cigarettes at a Yorkshire farm.

Michael Haley, 39, of Meadow Way, Walkington, Beverley; Rafal Miller, 37, and Grzegorz Kojak, 50, from Poland; were found with illegal tobacco products worth £3,041,476 in unpaid duty, an investigation by HMRC revealed.

HMRC officers caught the trio loading cigarettes into a van at the farm on Driffield Road, Huggate, York, in September 2018. The cigarettes were concealed inside metal containers, which were packed in cardboard boxes.

The men were arrested and 10,853,500 cigarettes were seized from the van, a warehouse on the farm and a lorry trailer parked inside.

One other man fled the scene and enquiries are ongoing into his whereabouts.

Brett Wilkinson, Assistant Director, Fraud Investigation Service, HMRC, said: "This was a deliberate attempt to flood the streets with illegal cigarettes and deprive our public services of millions of pounds. Hayley, Kojak and Miller thought their smuggling scam would go unnoticed – but they were wrong and now they are paying the price."

The trio admitted excise fraud at Hull Crown Court in March 2019. They were sentenced at the same court in December 2019. Haley was sentenced to three years and nine months in prison; Miller to three years and nine months; and Kojak to three years and three months.

HMRC knocks out promoter who used own avoidance scheme

Designer of the Root2 Tax Ltd avoidance scheme was beaten at the First Tier Tribunal by HMRC

HMRC has won a significant First Tier Tribunal case involving a tax avoidance promoter, Root2 Tax Ltd, that used an avoidance scheme designed and promoted by themselves.

The result could lead to the recovery of £2.4 million in tax and National Insurance Contributions (NICs) in this case, with a further £110 million in related cases.

The firm's Alchemy scheme involved an employee entering a high-risk form of gambling, known as spread betting. The scheme's intended result was a tax-free betting win for the individual employee, which was taken instead of taxable employment income, and a tax-deductible expense for the company.

HMRC defeated the avoidance scheme at the First Tier Tribunal, arguing that the scheme's main purpose was to provide tax-free employment income that should have been subject to PAYE and NICs. The tribunal agreed with HMRC, and decided that the payment made by the company represented income from the employment of the employee, and should have been taxed accordingly.

The judge also agreed with HMRC's argument that disguised remuneration legislation would apply to the arrangements. This legislation was introduced in 2011 to challenge PAYE avoidance schemes. The judge found that it would apply as an alternative to the income from employment decision.

Mary Aiston, Director of the Counter Avoidance Directorate, said: "This was an excellent win against a promoter who used their own avoidance scheme to try to take their profits tax free. The defeat of the Alchemy scheme shows that the department will tackle the people who sell these schemes head-on, ensuring that they do not escape paying the tax they owe.

"There should have been no doubt that this convoluted scheme – where employment income came as a tax-free betting win – was too good to be true. Our message to people tempted by a tax avoidance scheme is, if something looks too good to be true, then it almost certainly is."

HMR previously succeeded in litigation against Root2 Tax Ltd for the non-disclosure of the Alchemy scheme under the Disclosure of Tax Avoidance Schemes rules.

Further information

- Alchemy is a scheme that is intended to allow selected employees (usually directors) to receive income tax-free, paid for by an expense incurred by the company.
- The scheme relies on the idea that the employee is involved in a high-risk form of gambling known as spread betting. The employee hedges the bet with another contract known as a call spread option. This mitigates the risk for the employee. The option and its financial responsibilities are subsequently transferred to the employer.
- The Directors of Root2 developed Alchemy, marketed it and used it themselves. The intended result of the scheme was a tax-free betting win for the individual employee, rather than taxable employment income, and a tax-deductible expense for the company on its payment to take over the CSO.
- In September 2017 the FTT confirmed that Alchemy was disclosable under the Disclosure of Tax Avoidance Schemes (DOTAS) rules. That Tribunal decision considered only whether Alchemy was notifiable. This hearing has confirmed Alchemy does not work.
- This is the first time HMRC has litigated using the findings established by the Supreme Court in the high-profile 'Rangers' case, and applying those findings to non-loan arrangements. 'Rangers' provided final clarity on PAYE avoidance that typically utilised Employment Benefit Trusts as part of the arrangements. This new decision builds on the findings in 'Rangers', applying the principles into PAYE avoidance that utilised the directors' use of their own company for avoidance purposes.
- The disguised remuneration legislation was introduced in 2011 to challenge contrived PAYE avoidance schemes. It takes HMRC significant amounts of time to investigate these complex avoidance schemes and prepare for litigation, and this is the first time this legislation has been used in a Tribunal case. The disguised remuneration legislation can be found at Part 7A of ITEPA 2003.