Quantum of risk

Management of taxes



01 January 2016

Anton Lane describes how advisers can manage their own and a client's risks when HMRC opens an enquiry

Key Points

What's the issue?

Now that HMRC is using intelligence to actively target tax planning, advisers should be aware of the risks

What does it mean to me?

The duty of care an adviser has to their client heightens the threat of unforeseen risks

What can I take away?

Manage risks by objective review, internal procedures, a proactive approach and using independent advice

Any firm renewing its professional indemnity insurance will know that the cost of tax advice cover has increased. The reason? HMRC is actively targeting many areas of tax planning and perceived areas of tax risks, resulting in a higher possibility of complaints and claims on professional insurance.

Some firms may consider that they have not provided a client with tax advice and instead have chosen to introduce an expert. This is often the situation when an accountant has become aware of a tax planning opportunity (a tax scheme or innovative structure) that suits a particular client. However, advisers should be warned that clever litigators are likely to consider the extent of an adviser's duty of care.

A particular risk that springs to mind is if correspondence shows that an adviser has introduced and recommended the use of a particular tax scheme. In this situation, the client may consider their trusted adviser has given the planning their seal of approval. What if an adviser did not consider or was not aware of the options available? The adviser may not have an obligation to consider all of them but they may have a duty to suggest that either they or the clients do.

When it comes to investigations, the extent of the adviser's involvement with introducing a client to an opportunity will inevitably affect their risks.

The adviser with just one client that has undertaken schematic planning (as opposed to an adviser with a large percentage of clients using planning for consecutive years) may be at lower risk from:

- claims on insurance;
- complaints to professional bodies;

- increased information passing to HMRC;
- potential damage to reputation; and
- potential loss of business.

These risks are not limited to schemes that have been implemented. The same risks can arise if a client under enquiry feels that identified errors ought to have been managed by the adviser.

Also, many clients look to their adviser to manage an enquiry and resolve issues with HMRC. If the enquiry is handled poorly from the outset, a client may contend that the adviser caused more problems for them by the manner they adopted with HMRC.

Where penalties are arguably higher as a result, the threat of the risks set out above is more prevalent.

Managing risks

When an enquiry opens, what has happened cannot be changed. It is necessary to consider what is done now to manage risks.

1 – Review the enquiry

HMRC rarely opens an enquiry for the joy of taking an uncalculated review of a taxpayer. Nowadays, enquiries originate from HMRC's Risk and Intelligence Service (RIS) whose staff spend their days playing with their award-winning software, CONNECT.

When a letter opening an enquiry is received, it is important to consider the request for information and to which tax irregularity it could relate. An opening letter may not always indicate where the enquiries are going. It may be structured simply to alert the taxpayer that HMRC is investigating to give them the opportunity to make a disclosure.

Most advisers cannot place themselves in HMRC's shoes, having had no experience in investigative techniques. If they have potential conflicts of interest they may not want to.

2 – Internal review

Having identified the possible reasons for the line of enquiry, an adviser should consider these questions:

- What are the terms of your engagement and is your position limited where you have introduced an expert?
- Are the services you have provided included within the parameters of your engagement?
- Have you provided full advice to include the options available to the client?
- Do you have any conflicts of interest?
- Do you have the experience and technical expertise to manage the enquiry?
- Is there a requirement to notify insurers (both fee protection and professional indemnity)?
- Is there a money laundering reporting obligation?
- Should a tax risk specialist be approached?
- In light of all facts, is it in the client's best interest that the adviser acts in relation to the enquiry?
- Is the engagement letter in place sufficient to act in relation to the enquiry?

It would be prudent to formally note first that the above have been considered and, second, the outcome of those deliberations. Often it is worth holding a separate risk meeting to consider the questions objectively. For larger firms, it may be prudent to form a risk committee to approach these questions independently and record its findings. This approach, although appearing bureaucratic, shows professional bodies and insurers that systems are in place to monitor risks and manage situations should client complaints occur.

The approach also forces an adviser to be objective and, it is to be hoped, put conflicts to one side to consider the client's best interests.

3 – Managing enquiries

It would be prudent to consider the timescale with which to respond to HMRC if we can assume the following:

- no conflicts of interest;
- relevant experience of managing enquiries and dealing with HMRC;
- technical expertise;
- satisfied advice given was complete; and
- resources are available to manage and deal with the enquiries.

A notice is normally accompanied with a request to respond within 30 days. However, this is the minimum period required and it may not be practical to respond within the timeframe. Is it sensible to request 60 or 90 days to respond given we would generally suggest that at the outset of an enquiry these activities are undertaken:

- review client files to establish potentially contentious areas;
- analyse business performance over a period of time;
- identify tax planning undertaken;
- establish all corporate interests;
- establish whether PAYE/VAT business interest audits, enquiries and reviews have happened; and
- meet the client to discuss possible areas of irregularities.

We often make forensic studies of prospective clients before meeting them. It is amazing what information is available and, combined with our experience, it enables us to pre-empt areas of tax concern.

Telephoning the HMRC officer before the client meeting may also be beneficial. It will demonstrate the seriousness an adviser and client are taking towards the enquiry. It will also explain the rationale for extending the response time – an example being availability to hold the meeting.

Care must be taken during the call not to make any indications relating to tax exposure or areas being considered. However, it is always useful to request of the officer specific issues they would like you to consider with the aim of fully cooperating and efficiently reporting back. The officer will normally assert that it is for the taxpayer to disclose any irregularities, although they may let slip one or two broad areas of interest.

The risk areas can then be discussed with the client – preferably at a meeting. Often the client will bring to your attention areas where there could be tax irregularities. It is worth noting that seldom are all released immediately.

It is important to document what is discussed at the client meeting. The following can be confirmed in subsequent written correspondence:

- the implications of not disclosing tax irregularities to HMRC to include increased penalties and, in the event of suspected fraud, the possibility of criminal

investigation and prosecution;
- it is often useful to discuss how HMRC can access information without a taxpayer’s knowledge;
- the initial areas the client has set out, which may have tax irregularities;
- areas where the adviser has concerns and requests the client to consider in more depth; and
- whether, given the initial review, what code of practice the enquiries or disclosure should fall under.

It will then become apparent that the adviser has placed themself in a more comfortable position to enter into communications with HMRC or make a disclosure.

If there are tax irregularities, we suggest presenting all of them to HMRC instead of answering its questions and the officer arriving at a conclusion. The adviser would prepare a disclosure report adopted by a client and the case presented. The advantages are:

- it manages time better instead of reacting to HMRC’s queries;
- technical arguments can be presented;
- penalty mitigation is likely to be greater as a result; and
- through the process, other irregularities may come to light – better the client and adviser bring them to HMRC’s attention before they discover them.

Many enquiries appear simple at the outset only to develop unexpectedly, consuming the adviser and client; the approaches suggested here should help to prevent them being escalated.