

Risky business

Danielle Ford runs the rule over HMRC's compliance risk review process

HMRC has always carried out a large volume of compliance activity through enquiries and interventions each year, which have historically been either random or information led. Now, with the array of sources and the huge volume of information HMRC possesses, random enquiries are becoming a thing of the past.

Settlement of enquiries and HMRC's handling of enquiries is never far from the press, but something less talked about is the review work and analysis HMRC undertakes before an enquiry is commenced.

Much of HMRC's analysis is centralised within the Risk & Intelligence Service (RIS) department who have access to all data and information which lead to an enquiry. This information is used to assess the tax risks or areas of concern for all taxpayers.

RIS usually undertake an analysis of a particular taxpayer under three circumstances:

1. An aspect of their tax affairs has raised a flag on HMRC's various systems.
2. Intelligence has been received.
3. The taxpayer fits within a category of taxpayer for which HMRC has an active compliance campaign (for example Chinese takeaways).

In some cases, individual HMRC officers may have identified a risk themselves and requested a risk review be undertaken – this is a practice used within the Fraud Investigation Service (FIS).

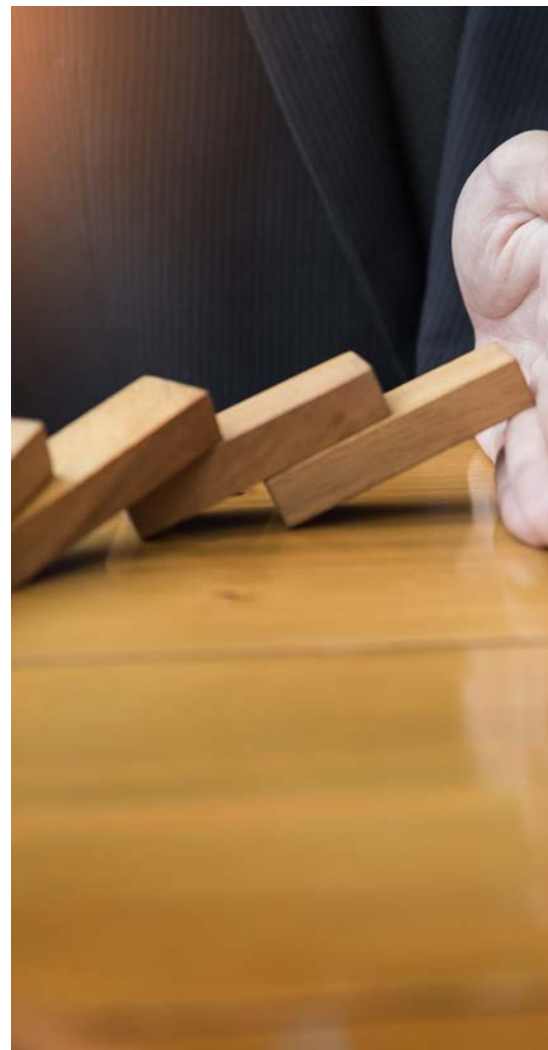
Sources of information

Not only does HMRC have possession of and access to

more information than ever before, the accuracy and detail have vastly improved. It would be impossible for HMRC officers to risk and interpret this; accordingly, HMRC has a proprietary Connect software to assist. Connect is incredibly powerful and is used to analyse all information HMRC holds on its various databases, highlighting connections such as all bank accounts, companies, properties and online selling platforms the taxpayer is linked to.

Supporting Connect are HMRC's various internal systems and databases, including historic tax returns, as well as a powerful database of UK property information. The information held within the property database is incredibly detailed and accurate and is linked to the Land Registry. As a result, HMRC holds full details of transactions in land and property, including sale and purchase parties, dates of transactions and amounts involved. Many HMRC investigations have been commenced based on a means risk identified by comparing a property purchase to declared income in tax returns.

In addition to this, HMRC receives significant information from jurisdictions around the world, under the Common Reporting Standard (CRS); the automatic exchange of international data sharing means HMRC is given financial information provided by overseas financial institutions on those who have a UK address, which includes their account numbers, balances, income received and disposal proceeds.



This information is usually the source of nudge letters to those affected; however, instances with the largest potential tax losses are selected for a formal investigation.

Let's not forget open-source information. This can include more obvious avenues, such as Companies House, Zoopla or Rightmove, but also the use of Google Maps to view the exterior of a taxpayer's property and any improvement works and their vehicles, plus social media to gain an understanding of their lifestyle.

Is the risking process infallible?

With all of this information available to HMRC, which is collated and analysed by specialist teams, one would expect the job of a tax inspector to be simple. However, that is not always the case. There can be errors in both the underlying



data, as well as the interpretation thereon. Identified risks still require the critical review of HMRC's trained investigators to bring a (hopefully) common-sense approach.

To illustrate this, the incredibly detailed data HMRC owns about property ownership and transactions links this to a taxpayer by name. The HMRC software identifies and collates this detailed information. However, where two or more taxpayers have the same name, anomalies can arise; therefore, the need for review by the inspector before an enquiry is raised.

In an example of a case selected for enquiry, the risk package focused on only one year, when there was concerns over an individual's means to afford the property they had just purchased. In this particular

instance, the software had compared the individual's salary to likely monthly mortgage payments and ability to save the level of deposit required for a 10% or 20% down payment, but had completely overlooked a seven-figure bonus in a prior tax year.

Furthermore, the overseas financial information HMRC receives is often reported incorrectly by the financial institution; for example, an account balance being reported as income, leading HMRC to believe a large insufficiency of tax has been paid. A further example we have seen is a case where an overseas bank account was part of a discretionary trust structure, but the report to HMRC was made based on the UK resident beneficiary being the owner of the account, leading HMRC to incorrectly conclude the beneficiary has underdeclared their income or gains.

Going a step further, the overseas information can be incorrectly interpreted, even if the data itself is accurate. We have seen cases where the income or gains have already been reported but are still queried by HMRC. This can be because the specific amount could not be reconciled. This can occur for a number of reasons, typically currency conversion or calendar year reporting, with two UK tax years crossed over or grouped together with other income or gains in the tax year on the return. In some cases, HMRC's review (or lack thereof) of the tax return has missed the entry entirely.

In conclusion, in some cases, an HMRC investigation will not have a solid foundation. However, the likelihood of this decreases as HMRC refines its data sources and methods. It has never been more likely that HMRC holds information on an individual that will allow them to

correctly assess and challenge a tax position.

How can I protect my position?

If you receive an HMRC enquiry it is now highly likely it will be based on information held and/or a tax risk which has been identified. It can be seen therefore that if the enquiry process is not managed in the correct way this can have a huge impact on the outcome of the enquiry, both in terms of the duration of the enquiry and also the level of penalty which may be applied to any errors or omissions discovered. Seeking professional advice on receipt of an HMRC enquiry is recommended in order to protect your position and to resolve the enquiry in the most efficient way.

Should you discover an error or mistake in your tax filings or discover you potentially should have reported income or gains when you have not, we strongly recommend making a disclosure to HMRC – before they contact you.

A disclosure before any HMRC contact is considered 'unprompted' for penalty purposes, granting access to the lowest possible penalties, in some cases, as low as 0%. Furthermore, there is a clearly defined process for making disclosures to HMRC, which carries advantages in a much shorter timescale to completion, compared to a full enquiry which can take many months or years to conclude.

Seeking experienced professional advice is of paramount importance; your adviser will be able to guide you through the process from start to finish and help ensure a successful and timely outcome.

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