A better way of handling HMRC enquiries and disputes

The landscape for managing tax enquiries and disputes has changed significantly in recent years and HMRC has published its internal guidance which sets the template for how HMRC will use a Collaborative Dispute Resolution (CDR) approach as it carries out its tax compliance work. In this alert, our tax dispute resolution experts:

- Explain how you can use the new guidance to get better outcomes from HMRC enquiries and disputes
- Set out some practical examples of how we have helped clients to resolve disputes using CDR
- Provide an overview of the breadth of support we can provide to help businesses and individuals benefit from this new approach.

What is ‘collaborative dispute resolution’?

HMRC’s Litigation and Settlement Strategy (LSS) has been relaunched with detailed guidance setting out how HMRC should conduct compliance checks to ensure that risks are resolved as efficiently as possible. Where HMRC is in dispute with taxpayers, the LSS and the guidance set best practice for reaching a settlement and avoiding a costly and uncertain litigation process. This new approach is applicable across all taxes and duties, so the guidance applies equally to any tax dispute or enquiry, regardless of the tax or the HMRC office dealing with the issue.

The approach in the guidance is underpinned by ‘collaborative dispute resolution’. A collaborative approach is where both parties recognise a shared interest in resolving the dispute cost effectively and bring a shared mindset focused on resolving the dispute on satisfactory terms. HMRC’s guidance describes a CDR approach as including:

- Sharing details of the perceived tax risk and clearly articulating the point in dispute
- Both parties agreeing the key questions which need to be answered to resolve a dispute (i.e. establishing a ‘decision tree’)
- Reaching a shared understanding of what will be the relevant facts to answer those key questions
- Jointly agreeing a timetable with key milestones and target dates for an enquiry

"Where a dispute has reached an apparent impasse, it is still possible for the parties to work collaboratively in order to try to unlock the process...Similarly, parties should not stop working collaboratively simply because one (or perhaps both) consider(s) that a dispute can ultimately only be resolved by litigation."

HMRC’s Commentary on the Litigation and Settlement Strategy
Discussing, sharing and jointly testing tax technical arguments to assess their relative strengths and weaknesses, and exploring possible interpretations of the facts/relevant law which might give different outcomes.

Using a third party (e.g. a mediator) to help both parties resolve disputes cost effectively and efficiently.

Working together to support expeditious litigation, where that is necessary.

To supplement this approach, HMRC launched a pilot to explore whether Alternative Dispute Resolution (ADR) – in particular the involvement of a third party mediator (and a specific subset of CDR) – could be used to help resolve tax disputes, especially those where progress had stalled or were heading towards litigation when avenues for settlement had not yet been exhausted. The ADR pilot has been considered a huge success by HMRC and clients alike and HMRC is now beginning to apply ADR more widely.

Whilst the CDR approach has shown it can significantly reduce the costs of managing enquiries for all parties, in many instances HMRC caseworkers are still adopting the ‘old’ approach to enquiries, for example issuing large requests for information without explaining the risk and then forming their own view of the tax treatment without a dialogue with the taxpayer. This can lead to an adversarial approach and make dispute resolution more difficult.

Our experience is that it is open to clients to take the lead in encouraging a CDR approach, and that where those are adopted the results benefit all parties. On the next page are some examples of how we have supported clients in getting better outcomes through CDR.

"HMRC will always consider whether something which initially appears to be an 'all or nothing' issue is genuinely all or nothing or is in fact a case where there is a range of possible figures for tax due."

HMRC's Litigation and Settlement Strategy

How Ernst & Young can help

The cases studies on the following page illustrate how Ernst & Young's experts have used CDR to obtain great outcomes for clients. The scope of the support we can provide is broad, ranging from coaching clients on proposed approaches to HMRC to a full ADR process where we aim to conclude more complex disputes within six months. If you are currently involved in a dispute with HMRC and are not happy with the progress being made, or simply want to hone your dispute resolution skills for the future, we would be happy to discuss with you how we can help.

The following provides some examples of the breadth of the support we can provide business and individuals -

- Workshops with client tax teams to develop good CDR skills and techniques through role play tax dispute case studies

- Workshops to brainstorm current disputes, develop a preferred dispute resolution strategy and support the client to get the best CDR approach from HMRC.

- Reviewing issues which have been deemed ‘all or nothing’ to identify alternative approaches which may be acceptable to HMRC under the Litigation and Settlement Strategy.

- Supporting clients in working with HMRC to ensure CDR best practice is followed, and helping clients use CDR to get speedy and satisfactory resolution to their open enquiries and disputes.

- In substantial disputes where an impasse has been reached, regardless of whether the dispute is already in a litigation process, we can support clients to reach a resolution or narrow down their differences with HMRC through a formal ADR process.

"Minimising the scope for disputes, and reducing the costs to HMRC of resolving disputes is likely also to reduce customer costs, improving the customer's experience and making the UK a better place to work and do business."

HMRC's Commentary on the Litigation and Settlement Strategy
Our experience of collaborative dispute resolution – some examples

Case Study 1
Taking a hands-on approach in supporting clients to access the benefits of HMRC’s ‘best practice’ approach can achieve remarkable results in a short space of time:

A company had been in dispute for several years with HMRC over the 1982 valuation of an asset. The company was convinced that the asset had a substantial value in 1982 giving rise to a nil capital gain; HMRC was convinced of precisely the opposite.

We supported the client in making proposals to HMRC for a collaborative process. The process involved both parties working together to understand why they differed so radically, starting with points of agreement, then moving on to joint agreement of a methodology or ‘decision tree’ for resolving differences, then jointly testing the evidence and arguments in favour of differing positions.

This approach led to the resolution of the dispute within a single three hour meeting on a basis which both the company and HMRC accepted was a reasonable expectation of what would have been obtained from litigation. In this case, the joint development of a ‘decision tree’ was key – it forced both sides early on to confront the difficult but essential point of what was the most appropriate valuation methodology.

Case Study 2
The benefits of collaborative working are not confined to major disputes and do not necessarily involve an elaborate process – they can help wherever a dispute seems to be ‘stuck’ or appears to be headed off the rails:

HMRC was enquiring into a company’s returns and had already issued a wide-ranging and resource intensive information request. On a call to HMRC, we secured HMRC’s agreement to approach the enquiries collaboratively, and to start by setting out its view of the tax risks in question. One of the risks was about a change in accounting policy. We discussed whether HMRC saw this as a move from a valid to an invalid basis of accounting, or from one valid basis to another valid basis.

The other risk – also leading to extensive information requests – was a Transfer Pricing one, where we pointed out that the counterparty was UK resident and had returned the results in full for UK tax. Challenged on both these points, the HMRC officer agreed to reflect, and came back a few days later with closure notices withdrawing the enquiries altogether.

Case Study 3
A collaborative approach can add great value even where litigation has started:

A UK FTSE 250 group was in dispute with HMRC on a VAT issue that was headed for litigation – with Tribunal dates set and voluminous document bundles already exchanged. Another advisor had been leading the enquiry for some 3 years, before we were instructed to review the issue and try to resolve the matter collaboratively.

Taking a collaborative approach to the issue, despite the length of time it had already been under enquiry, started with making sure everyone had a good grip of the facts. We did this though an interactive session around a whiteboard, changing the diagram of the transactions, and the relevant labels, until everyone was happy that it reflected the transaction as they understood it. That took about two hours, after which the HMRC technical expert said spontaneously that more progress had been made in those two hours than in years of enquiries to date.

The whiteboard session managed to narrow down the issues to a single question which turned mainly on the operation of trust law, and we jointly agreed on a further piece of analysis on that trust law point which allowed the dispute to be settled to the satisfaction of both parties. This saved HMRC and the taxpayer the costs – and uncertainty – of a tribunal appearance which could have lasted three or four days.

Case Study 4
Where an impasse has been reached, ADR can provide a process to get the parties to tackle the dispute with a fresh approach and find a way through:

A company had been involved in a major VAT dispute with HMRC which had been running since 2004. The issue stemmed from a complex valuation point which fed into the output tax calculation. It was accepted by the parties that it was extremely difficult to obtain a correct answer on the issue but, whilst the technical treatment was not in doubt, the valuation point could not be agreed. Previously, an adversarial approach had led to both parties proposing valuation methodologies which the other side had rejected. After seven years an impasse had been reached and, despite having already been to the Tribunal once on the issue, the parties were unable to reach agreement.

We were asked to assist the client in early 2011. We were able to secure HMRC’s agreement that the case was suitable for ADR and engaged in a process which within six months had resolved this long running dispute and agreed a methodology for the future to prevent the dispute arising again. Key to the success was adopting a new collaborative way of working.

Rather than each party formulating their own view of the answer to be challenged by the other, we instead started afresh and worked on building a new methodology together which was acceptable to both parties. Whilst third party mediation was envisaged as part of the process, this did not prove necessary to unlock the dispute.
Why Ernst & Young?

Our Collaborative Dispute Resolution team consists of three mediators accredited with the Centre for Effective Dispute Resolution and with significant insight and experience of collaborative dispute resolution both in HMRC and at Ernst & Young.

Further information

Geoff Lloyd
Geoff was previously Director of Dispute Resolution at HMRC where he was responsible for developing HMRC's collaborative dispute resolution approach and the new LSS and its accompanying guidance.

Geoff specialises in supporting and advising clients in handling HMRC and HMRC enquiries and resolving tax disputes through collaborative working and ADR.

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Jim Wilson
Jim was on secondment at HMRC's Dispute Resolution Unit for nine months working on the ADR pilot and writing the new LSS.

Jim has extensive experience of working with a wide range of clients (both corporate and individual) in managing and successfully resolving significant tax disputes with HMRC.

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Paul Dennis
Paul trained as an Inspector at HMRC and has successfully managed three cases through the ADR process as well as resolved numerous disputes which had reached an impasse using CDR techniques.

Paul assists clients in obtaining successful outcomes from interactions with HMRC, including SAO certification support, enquiry management, penalty negotiations and settlement negotiations.

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