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Chair, Economic Affairs Finance Bill Sub-Committee  
House of Lords  
London  
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19 February 2021

Dear George

**GOVERNMENT RESPONSE TO THE HOUSE OF LORDS ECONOMIC AFFAIRS REPORT,  
NEW POWERS FOR HMRC: FAIR AND PROPORTIONATE?**

I am pleased to attach a comprehensive Government response to the Sub-Committee's report, *New Powers for HMRC: Fair and Proportionate?*, published in December 2020.

A healthy and effective tax system relies on trust. HMRC have a vital role to collect the tax that pays for public services and taxpayers must be able to trust that HMRC act fairly, effectively and professionally to ensure that everyone pays the tax that is due. Maintaining and building this trust is an important part of the Government's approach to tax administration reform.

HMRC have powers, approved by Parliament, to secure through taxation the funds for public services. This also requires them to tackle the minority of people and businesses who seek to avoid or evade tax, so providing a level playing field for the overwhelming majority that pay their taxes.

In preparing this response, the Government has considered the issues that the Sub-Committee has highlighted carefully. As you will see from the detailed response which I enclose, HMRC have already taken forward a number of actions as a result of your report, such as continuing to look for new approaches to tackling promoters of tax avoidance, and taking forward work on providing greater protection for those currently using unregulated tax advisers.

I am pleased to say that the Government has accepted nine recommendations and partially accepted six. I am grateful to you and your Sub-Committee for its careful consideration and reflections on these important issues.

The Government believes it remains important that HMRC have the powers necessary to identify those who pay less tax than they should and, where this is the case, to intervene appropriately in order to put things right.

I thank the Sub-Committee for its continued interest in this area.

As ever,

A handwritten signature in black ink, appearing to read 'Jesse' in a cursive, flowing style.

RT HON JESSE NORMAN MP

House of Lords Economic Affairs Finance Bill Sub-Committee: New powers for HMRC: fair and proportionate? (HL Paper 198)

Government Response

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## 1. Introduction

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The Government thanks the Committee for its 4<sup>th</sup> report of session 2019-21 and notes its conclusions and recommendations.

A healthy tax system relies on trust. HMRC have a vital role to collect the tax that pays for public services, and taxpayers must be able to trust that HMRC will act fairly, effectively and professionally to ensure that everyone pays the tax that is due. Maintaining and building this trust is an important part of the Government's approach to tax administration reform.

HMRC have powers, approved by Parliament, to collect the tax that is due, including by tackling the minority of people and businesses who seek to avoid or evade paying their tax, so providing a level playing field for the overwhelming majority who willingly pay what they owe.

Since 2010, the Government has introduced over 100 reforms to continue to tackle tax avoidance and evasion. Of these, over 40 have strengthened HMRC's powers to administer the tax system, enhancing their ability to detect those who pay less than they should, investigate efficiently and enforce compliance effectively and proportionately.

Alongside these reforms, the Government supports HMRC in maintaining and developing a culture that ensures all taxpayers are treated fairly and empathetically, taking account of their circumstances and needs. This means ensuring that the correct tax is paid by helping those who try to get it right, resolving disputes by agreement wherever possible, and taking enforcement action, with appropriate safeguards, against those who HMRC believe are trying to pay less than they owe.

HMRC recently published their evaluation report on the implementation of powers, obligations and safeguards introduced since 2012. HMRC worked closely with representatives of taxpayers and agents to carry out this evaluation. The evaluation underlined the importance of the work HMRC are doing to build and maintain public trust in the tax system, including through the wider powers and safeguards programme set out by the Financial Secretary to the Treasury in July 2019 and the Government's response to Sir Amyas Morse's Independent Loan Charge Review.

The evaluation has also highlighted new opportunities for HMRC to improve public trust in the tax system. These include: deepening engagement with voluntary and community services to help raise awareness of tax obligations among harder-to-reach taxpayers; taking steps to enhance public confidence in HMRC's governance, decision-making and operations; and improving guidance, for example on the application of "reasonable excuse" provisions.

HMRC are taking forward 21 commitments to address the findings of this evaluation. This work will support the Government's vision for a tax system fit for the 21st century: a system that provides a better experience for taxpayers while reducing the tax gap and also building greater resilience and responsiveness to future national crises.

The remainder of this memorandum will address and respond to the recommendations made in the Committee's report.

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## 2. A principled approach to powers

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*Recommendation 1: We believe the Government should have awaited the outcome of its own review into the operation of its powers and safeguards before further powers were proposed for HMRC. The outcome of its review should have been used to inform and frame the draft Finance Bill proposals. Evaluation of what has gone before must always be a useful means to determine the best way forward.*

### **The Government does not accept this recommendation.**

HMRC's evaluation report titled "HMRC's implementation of powers, obligations and safeguards introduced since 2012" was published on 4 February 2021.<sup>1</sup> The evaluation followed the Committee's December 2018 report "The Powers of HMRC: Treating Taxpayers Fairly". That report recommended a Powers Review that "could take an overview of the development of HMRC powers since 2012, and their cumulative effect, making the case for change, for new principles or additional safeguards".

As set out in the Financial Secretary to the Treasury's Written Ministerial Statement on HMRC Powers and Taxpayer Safeguards, the Government concluded that a full review of HMRC powers is not necessary at this time<sup>1</sup>. The powers granted to HMRC since 2012 were properly scrutinised before being granted by Parliament. The Government's view is that they remain necessary and proportionate.

The Financial Secretary did, however, ask HMRC to evaluate the implementation of powers introduced since 2012 in relation to the powers and safeguards principles, engaging with stakeholders, including taxpayers and their representatives. The evaluation report underlines the importance of the changes HMRC are already introducing to help build and maintain public trust in the tax system, including through the wider powers and safeguards programme as set out in the Written Ministerial Statement of 22 July 2019, and the Government's response to Sir Amyas Morse's Independent Loan Charge Review.

HMRC continue to identify new areas where the ever-changing risks of tax avoidance and evasion threaten the collection of taxes needed to fund essential public services. It is therefore appropriate that the Government continues to take action to address these areas as they arise. The Government would not want to risk losing revenue while the evaluation work was concluding. Nonetheless, the commitments made in the report will apply to the implementation of new powers, as it does to those introduced since 2012.

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<sup>1</sup> <https://questions-statements.parliament.uk/written-statements/detail/2019-07-22/HCWS1785>

### 3. Tackling promoters of mass-marketed tax avoidance schemes

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*Recommendation 2: We recommend HMRC revisits the triggers for POTAS to minimise the risk of these rules affecting bona fide professional advisers. Specifically, we question whether DAC6 should be a trigger for a POTAS, particularly given the assurances HMRC appears to have given stakeholders that DAC6 would not feed into other areas of the UK tax code. (Paragraph 46)*

#### The Government accepts this recommendation.

The Government and HMRC are committed to tackling those who promote tax avoidance schemes. HMRC use a range of powers to achieve this, including the Promoters of Tax Avoidance Schemes (POTAS) legislation. POTAS is designed to encourage promoters, generally someone who designs or markets the tax avoidance scheme or is responsible for its organisation, to change their behaviour voluntarily or face an escalating series of sanctions. The effectiveness of the POTAS legislation is kept under constant review.

HMRC consulted on amendments to the POTAS regime between 21 July and 15 September 2020. A formal response will be published in due course.

Following the end of the UK's EU exit transition period, in line with The International Tax Enforcement (Disclosable Arrangements) (Amendment) (No. "2) (EU Exit) Regulations 2020<sup>2</sup>, DAC6 no longer applies to certain categories of reporting in the UK. As a result, the Government agrees that it is no longer appropriate to include DAC6 as a POTAS trigger.

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<sup>2</sup> SI 2020/1649 <https://www.legislation.gov.uk/uksi/2020/1649/made>

**Recommendation 3:** *Although the evidence we heard suggests the proposed measures to target promoters are worth pursuing, we are unconvinced that they will be sufficient to drive the hard core out of business. The Government should continue to look for new approaches to tackling promoters. (Paragraph 53)*

### **The Government accepts this recommendation.**

The Government is committed to continue to tackle promoters of tax avoidance schemes and has taken action through the introduction of robust measures to tackle their activities. The new measures announced at Budget 2020, and subject to consultation from 21 July to 15 September 2020, will strengthen the existing regimes and help HMRC take action more swiftly against promoters. On 12 November 2020, the Government also announced that it will consult this spring on a further package of measures to ensure promoters face stronger sanctions more quickly.

The Government and HMRC accept that a wide-ranging approach is needed to tackle promoters. On 19 March 2020, HMRC published a strategy for tackling promoters of mass-market tax avoidance, which sets out HMRC's work to date and outlines how HMRC will continue to take robust action against promoters of tax avoidance. The Promoter Strategy is available on GOV.UK.

In 2019-20 HMRC doubled the resources committed to tackling promoters and their supply chains. HMRC use all the powers it has available to disrupt their business models, including appropriate use of criminal and civil powers.

HMRC are also collaborating with partner bodies to tackle promoters. For example, HMRC refer promoter companies and their directors to The Insolvency Service, where appropriate, so they can consider whether to take action on the grounds they are not trading in the public interest. HMRC have been working closely with the Advertising Standards Authority (ASA) resulting in three successful complaints about misleading advertising, revised guidance about advertising tax avoidance schemes and the issuing of a joint HMRC/ASA enforcement notice in November 2020. Some promoters have already changed their advertising in response. Promoters are rarely members of professional bodies that have adopted the rules on Professional Conduct in Relation to Taxation (PCRT), but where they are, HMRC will refer them to their body where their actions are in breach of PCRT.

**Recommendation 4:** *The Government should keep the efficacy of measures under review, and not hesitate to respond swiftly if there is evidence that the hard core of promoters are continuing to frustrate HMRC's ability to stop the marketing of tax avoidance schemes. (Paragraph 54)*

**The Government accepts this recommendation.**

The Government will continue to monitor the efficacy of measures aimed at tackling those who promote or enable tax avoidance. HMRC actively monitor the avoidance market and prioritise work to tackle promoters.

The Government and HMRC are alert to developments in the avoidance market, for example, promoters are increasingly basing themselves offshore, which makes it harder for HMRC to act against them. On 12 November 2020, the Government announced it will consult this year on further measures to tackle promoters, building on the Promoter Strategy published on GOV.UK in March 2020. These proposals will include steps to address this behaviour.

***Recommendation 5:** ‘Naming and shaming’ is an important weapon in tackling the hard core of promoters; shining a light on their activities is key to ensuring HMRC’s warnings are effective. But it should only be used where clearly justified. The Government should revisit the safeguards in the draft Finance Bill to balance more effectively the importance of being able to name promoters against the risk of identifying the wrong people. (Paragraph 60)*

## **The Government does not accept this recommendation.**

The Government believes there is value in publicising details of schemes as early as possible, to give taxpayers the information they need to take informed decisions. Publicising details also deters taxpayers from becoming involved in avoidance schemes and makes it more difficult for promoters to sell those schemes in the first place.

HMRC can only name promoters and inform the public of their activities in limited circumstances as set out in legislation. For example, the Promoters of Tax Avoidance (POTAS) regime, which aims to change the behaviour of a persistent minority of promoters through a tough regime of penalties and monitoring requirements, has a number of inbuilt operational and legal safeguards ensuring only those who do not comply and change their behaviour can be publicly named.

The measures in the draft Finance Bill are not targeted at the vast majority of tax advisers who adhere to high professional standards. They are focused on high-risk promoters who seek to sidestep the existing rules or delay their impact. The proposed changes, as set out in the consultation document, include safeguards which are designed to strike the right balance between ensuring promoters have appropriate opportunities to make their case, and ensuring potential users of avoidance schemes are alerted to the risks as early as possible. The proposed changes to the disclosure regime (Disclosure of Tax Avoidance Schemes and Disclosure of Tax Avoidance Schemes: VAT and other Indirect Taxes) would give promoters a right of appeal against the issue of the Scheme Reference Number, which if successful would see their names withdrawn from publication. Ahead of naming, HMRC would also be required under the legislation to offer anyone they are considering naming the opportunity to make representations against being named.

This proposed change to the disclosure regime would also only be used when HMRC have reason to believe the scheme should be disclosed and the promoter has already failed to disclose it. The purpose of naming in this measure is to inform taxpayers and help them steer clear of these schemes, ensuring that they have as much information as possible and as early as possible, in order to make a judgement about the risks they might face if they get involved in a tax avoidance scheme.

**Recommendation 6:** *Taxpayers need to have better information about schemes so that they can see through a promoter’s sales pitch and recognise when they are being sold an aggressive tax avoidance scheme. A page on a website telling taxpayers how to identify a tax avoidance scheme is insufficient. HMRC must find ways to communicate directly with taxpayers; for example, there could be a single-page warning notice each year as part of its standard communications on self-assessment filing obligations. (Paragraph 73)*

*HMRC should be capable of planning a communications campaign to provide such warnings, without these warnings acting as a perverse incentive to take part in these schemes. It could look at what other agencies have done for guidance—for example, the Financial Conduct Authority’s communications regarding unscrupulous pensions advisers. (Paragraph 74)*

### **The Government accepts this recommendation.**

The Promoter Strategy, published in March 2020, made clear that HMRC would step up their communications to educate taxpayers to help them steer clear of avoidance schemes.

HMRC have always warned against engaging in tax avoidance and continue to publish ‘Spotlight’ communications when avoidance risks are identified. In April 2020, Spotlight 54 warned health workers returning to the NHS that avoidance scheme promoters were targeting them. HMRC shared this message widely with stakeholders including the Department of Health and Social Care, NHS Trusts and NHS Improvement as well as medical bodies. The issue was covered in national media and HMRC also used social media such as twitter and LinkedIn to convey these messages.

In November 2020 HMRC launched the ‘Tax avoidance: don’t get caught out’ communications campaign. The campaign is targeted at contractors and encourages them to stop and take time to check what they are signing up for, challenge what they have been told by those selling schemes, and protect themselves and others, by reporting schemes to HMRC. HMRC will continue with their communication activities, including exploring new opportunities to reach taxpayers who may be at risk of entering avoidance schemes.

HMRC will continue to deepen partnerships with voluntary and community organisations to help raise awareness of tax obligations amongst, and build trust with, harder to reach taxpayer groups. HMRC will also continue to explore opportunities for new and innovative communications approaches to help ensure that taxpayers, including harder to reach groups, understand their obligations.

***Recommendation 7:** We recommend that the Government collaborates with relevant specialists to decide what further steps could be taken to prevent disguised remuneration schemes being used by employment intermediaries. A first step would be to ensure that no government or public sector body contracts with an intermediary operating a disguised remuneration scheme, and to publicise this requirement along with the protocols that public bodies are expected to follow. (Paragraph 78)*

**The Government partially accepts this recommendation.**

The Government launched a call for evidence on tackling disguised remuneration tax avoidance that ran from 21 July to 30 September 2020. This sought views and evidence on issues including the drivers for the continuing use of disguised remuneration avoidance, and what further action the Government and HMRC can take to tackle this type of persistent avoidance. This included seeking views on promoters, employment supply chains and how HMRC can go further to help taxpayers steer clear of and leave avoidance schemes. HMRC are analysing the responses and plan to publish a summary of responses and next steps in due course.

**Recommendation 8:** *To be effective, the new measures depend on HMRC becoming aware of new schemes. We recommend that HMRC creates a dedicated tax avoidance reporting service which enables taxpayers and advisers to report schemes easily. HMRC should work with its communications team to ensure a high level of search engine optimisation for any online reporting service. Any information that helps close down a scheme or promoter should be highlighted by HMRC, with details anonymised. (Paragraph 82)*

## **The Government accepts this recommendation.**

Promoters of tax avoidance schemes are increasingly unlikely to disclose their schemes to HMRC so that they can continue to market them. HMRC use a range of activities to identify, monitor and track new avoidance schemes and the promoters behind those schemes, including using data, risk analysis and other intelligence gained from researching the avoidance market.

HMRC encourage anyone who is aware of avoidance schemes being marketed to provide HMRC with details so they can investigate and take action against the scheme and those promoting it. HMRC already have a dedicated service where taxpayers can either telephone or complete an online form to report a tax avoidance scheme. Information is treated in confidence and taxpayers do not have to provide their name, address or email address.

As is standard on GOV.UK, the page holding the details of the avoidance reporting service is optimised, so ensuring that it is prioritised in responses to online search requests. There are links to this page from other relevant pages, making it as easy to find as possible.

In addition, in November 2020 HMRC launched the 'Tax avoidance: don't get caught out' communications campaign. The campaign encourages contractors to report avoidance schemes via the online form or hotline. As part of this campaign HMRC have paid for messages to be placed on social media platforms and the Google search engine.

**Recommendation 9:** *We support greater protection for those currently using unregulated tax advisers, and recommend that the Government consults on options for how they might be regulated. We also recommend that HMRC works closely with the tax professional bodies on non-legislative action which can be taken in the interim to help taxpayers source reliable tax advice (such as a register of tax advisers) and to improve advisory material. HMRC should also consider what more it could do to support charities who provide tax advice. (Paragraph 98)*

## The Government partially accepts this recommendation.

Responses to the call for evidence<sup>3</sup> on raising standards in the tax advice market showed that, although the majority of stakeholders believed that action was required to raise standards, there were differing views on the form that action should take and on the strength of the case for regulation of this market.

The Government is mindful of striking the right balance between introducing new burdens on business and providing protection to those using tax advisers. Rather than moving straight to a fuller regulatory approach, as a first step the Government is exploring making professional indemnity insurance a compulsory requirement for tax advisers as a common minimum requirement for all tax advisers.

The Government believes that this:

- would allow market forces to drive up standards including potentially removing from the market those advisers who were unable, as a result of riskier practices, to obtain insurance
- would enable clients of unaffiliated advisers to have a method of redress should things go wrong and therefore improve taxpayer protection
- is well targeted, as initial costs to those already subject to some form of oversight, such as professional body members, and members of other regulated professions, such as financial advisers, are likely to be minimal.

The Government will consult on both the design of this proposal and also whether it best meets the policy intent. In line with the policy making process, responses to the consultation on that requirement and the Government's evaluation of the impact of the introduction of that requirement, should it proceed, will determine the next steps. An important element of any action is the scope of the population that this applies to, as stated in the next steps document<sup>4</sup> the Government will also consult on this.

As set out in the Raising standards in the tax advice market: summary of responses and next steps document published in November 2020, the Government has announced that HMRC will continue to work in partnership with the professional bodies (PBs). HMRC will work closely with PBs to understand the role they play in supervising and supporting their members and

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<sup>3</sup> <https://www.gov.uk/government/consultations/call-for-evidence-raising-standards-in-the-tax-advice-market>

<sup>4</sup> [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/934614/Raising\\_standards\\_in\\_the\\_tax\\_advice\\_market\\_-\\_summary\\_of\\_responses\\_and\\_next\\_steps.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/934614/Raising_standards_in_the_tax_advice_market_-_summary_of_responses_and_next_steps.pdf)

raising standards in the profession, as well as considering how HMRC could do more to inform taxpayers of the standards they should expect from their tax advisers. There are also opportunities as part of introducing a requirement to hold professional indemnity insurance, to consider options to improve transparency to help taxpayers make better choices when seeking tax advice.

HMRC recognise that charities are key to supporting vulnerable taxpayers and work closely with this sector including Low Incomes Tax Reform Group (LITRG), Tax Aid and Tax Help for Older People.

An example of how HMRC provide support to charities is through the Grant Funding to Voluntary & Community Sector (VCS) system. Each year, HMRC provide grant funding to VCS organisations to help support and provide advice to taxpayers who HMRC find it 'hard to reach'. For 20/21, HMRC ran a 1-year exercise after which HMRC took the decision to commit to a 3-year funding period for the years 2021-24, in recognition of the importance of this work. Successful organisations provide advice and support to people who need extra help understanding and complying with their tax obligations and claiming their entitlements.

#### 4. Civil information powers

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*Recommendation 10:1 : We recommend that: the requirement for tribunal approval for a third-party information request to a financial institution should remain;*

##### **The Government does not accept this recommendation.**

The UK plays a leading role in promoting international tax cooperation and transparency, and in developing international standards to ensure that all countries adhere to the agreed processes. To ensure international collaboration is effective, over 150 countries, including the UK, have agreed to international standards on exchange of information. This work is vital if international tax evasion and avoidance is to be tackled.

The UK will be unable to meet the international standard for exchange of information if the need for tribunal (or taxpayer) approval for a third party notice remains. HMRC rely on other countries providing information, and they in turn rely on the UK. Peer reviews of participating countries against these agreed standards have been a powerful driver for change; for example, leading to banking secrecy being abolished in over sixty countries. It is therefore important that the UK plays its part and meets these standards. Without removal of the tribunal process the UK would continue to fail to meet the international standards it is committed to. This is likely to lead to the UK failing this part of the standard in the next peer review process and there is a real risk that the UK's overall marking will drop from largely compliant (a "pass") to partially compliant (a "fail").

The proposed Financial Institution Notice (FIN) will allow the UK to meet the standard, while providing appropriate safeguards for taxpayers, and is in line with practice in all other G20 countries. Tribunal approval will still be required in any case where the taxpayer is not given a copy of the FIN.

The taxpayer safeguards built into the FIN include:

- HMRC may only issue the FIN where the information is reasonably required to check a known person's tax position, or in connection with recovery of a tax debt. This is an important safeguard for taxpayers that is very similar to the current legislation. It prevents FINs requiring irrelevant information or being used where there is no identified risk in what is known as a "fishing expedition". In fact, the international rules specifically say that fishing expeditions are not allowed.
- An authorised officer, experienced and specially trained in the application of civil information powers, must approve all FINs. This is another important safeguard for taxpayers. For instance, if the proposed FIN asks for irrelevant information the authorised officer will prevent it being issued. Authorised officers must pass an exam every 3 years to retain their status.
- For international requests it also has to be shown that the information is foreseeably relevant to the administration or collection of tax.

- The taxpayer will receive a copy of the FIN and a summary of reasons why the information is required. This notification requirement can only be disapplied by the tribunal on application by HMRC. This provision is the same as the one in the current third-party power.
- The third party can appeal against any penalties charged for failure to comply with the FIN.
- In addition, HMRC are required to make an annual report to Parliament on the use of FINs. The report will detail the number of notices issued and identify any issues arising from the use of the new notice. The annual report to Parliament will provide an opportunity to scrutinise HMRC's use of the new notices and will ensure that HMRC address any issues with their use. HMRC will seek representations from stakeholders when preparing the report so that Parliament can get a clear picture of the implementation of the new notices.

- *Recommendation 10:2: Financial institutions should have a right of appeal against any request they consider unduly onerous;*

**The Government does not accept this recommendation.**

The Government does not believe that a right of appeal is needed. The FIN is in line with practice in all other G20 countries and the law will prevent a notice being issued if the HMRC officer considers it would be onerous to comply with (many FINs are for routine documents such as bank statements). If a financial institution (or taxpayer) wishes to challenge a FIN they have the right to judicially review the decision to issue it. That is how tribunal approved notices are challenged at the moment - there is no right of appeal against such a notice under current rules. The financial institution can also appeal against penalties for not complying with a notice.

HMRC are strongly committed to working with financial institutions and representative bodies to ensure that they can confidently operate the new rules and processes without undue burdens. The draft legislation requires an annual report to Parliament to be made on the use of FINs. This reporting requirement to Parliament will be an important safeguard that will help identify any improvements that can be made in the use of FINs. HMRC will ensure that financial institutions are consulted in advance on the report to discuss their experience of the new power, and their views which will be included in the report. In preparing the report, HMRC will also seek representations from financial institutions and representative bodies.

HMRC will report on the operation of the FIN to their newly established Professional Standards Committee, which provides oversight of how HMRC administer the tax system and considers how HMRC's actions could affect trust in the tax system and public perception of fairness. HMRC will work with the Professional Standards Committee and its independent advisers to analyse and respond to, as necessary, any issues arising from the use of the powers.

- **Recommendation 10:3:** *The Government should clarify the interaction between the use of Financial Information Notices for debt collection and the direct recovery of debt provisions, and ensure that the safeguards for Financial Information Notices relating to debt are no less stringent than those for direct recovery of debt;*

**The Government partially accepts this recommendation.**

The new FIN and the direct recovery of debt (DRD) legislation are completely separate and the FIN will in no way affect direct recovery of debt. In particular a FIN cannot take the place of an information notice issued under the DRD rules. HMRC agree that this should be made clear and will cover it in the guidance for HMRC staff and external stakeholders.

The Government therefore does not think it is appropriate to compare the safeguards for FINs with those for DRD in the way suggested. DRD allows HMRC, in certain limited situations, to recover tax debts direct from the taxpayer's financial account. This is a very different power to the FIN and other information notices, which only allow HMRC to obtain information. DRD needs its own appropriate safeguards and it would not be proportionate or workable to apply all of these in the case of the FIN. For example, under the DRD rules, HMRC must have face to face contact with the taxpayer before proceeding. This is not appropriate for a FIN, which is an information power and not a power to recover tax directly from the taxpayer's account. In addition, the taxpayer may be resident in another country, and the tribunal may have decided the taxpayer should not be told about the FIN.

- **Recommendation 10:4:** *HMRC should review the whole process for dealing with international information requests requiring tribunal approval, working with financial institutions, the tax tribunal and others, to find other means of streamlining the process; and*

**The Government does not accept this recommendation.**

HMRC have already carefully reviewed the whole process, before and after proposing this legislative change, and have worked with the Ministry of Justice to streamline it, including: decreasing the time taken to allocate a tribunal hearing date; introducing standard templates to speed up the processes both internally and with treaty partners; and more than doubling the number of HMRC staff dealing with these requests. HMRC have also consulted publicly with stakeholders on this topic. While these improvements have been helpful, the Government has concluded that the UK is unable to meet the international standard without changing the current legislation to introduce the FIN. The FIN is consistent with practice in all other G20 countries.

- **Recommendation 10:5:** *Given the lack of consultation, HMRC should reconsider the implementation date. In doing so, they should undertake further consultation and communication to ensure that financial institutions are fully appraised of the implications of the measures and have sufficient time to prepare for them. Any revised implementation date should be determined in light of this consultation. (Paragraph 122)*

**The Government doesn't accept this recommendation.**

In accordance with Cabinet Office guidance on consultations, a full 12-week public consultation was run in 2018. Draft legislation was then published, with a response document, in July 2020 with an 8-week technical consultation period.

HMRC have also consulted informally and have had constructive discussions with representative bodies. HMRC remain committed to working with financial institutions and representative bodies to draft guidance on the FIN and ensure that they can confidently operate the new rules and processes without undue burdens.

## 5. Notifying uncertain tax treatment

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*Recommendation 11: When the Government consults on new proposals, it should clearly state its case and the evidence for it. This is common sense and is what the Government's Tax Consultation Framework requires. It is clear from our evidence that these requirements were not met by this consultation. We recommend that the Government should issue a new Stage 1 consultation, so it can work with business and representative bodies to develop a more targeted, proportionate measure than that now proposed. (Paragraph 136)*

### **The Government does not accept this recommendation.**

The consultation on this measure clearly stated the Government's case: that the tax gap contains a significant 'legal interpretation' element, more than half of which relates to large businesses, which this measure is intended to tackle and reduce. It will do this by providing HMRC with earlier and better information about legal interpretations being used by large businesses that may differ from HMRC's interpretation.

Respondents generally agreed that the legal interpretation portion of the tax gap needs addressing and agreed with the overarching policy objective, but felt that the proposed measure was not well targeted, and that the definition within it was too subjective. As a result of these concerns, which the Government understands and acknowledges, HMRC have been discussing a range of potential changes to the measure with stakeholders, aimed at making it clearer, more targeted and more proportionate. However, the Government does not believe it is necessary to issue a new Stage 1 consultation. Following these discussions, the Government will launch a further Stage 2 consultation and continue to work closely with businesses and representative bodies to ensure that the final measure is targeted and proportionate before publishing draft legislation for technical consultation.

***Recommendation 12:** While it is positive that HMRC has established a constructive relationship with most large businesses, it seems unnecessary and counter-productive to make a requirement to notify uncertain treatment apply to all, regardless of their risk status. We recommend that this new measure should be targeted only at the minority of large businesses that are of concern to HMRC. (Paragraph 141)*

**The Government partially accepts this recommendation.**

The vast majority of the large businesses who have a transparent, constructive relationship with HMRC will not be affected by this measure. They routinely discuss uncertain tax treatment issues with HMRC at Business Risk Review meetings. The next consultation will make it clear that where issues have been discussed in this way, there will be no requirement to notify them under this measure. The Government is also developing an objective test for uncertain tax treatment, which it believes should apply to all businesses within scope, rather than only those given a particular risk status under HMRC's Business Risk Review process, due to its inherent subjectivity. Further consultation will however test the scope for reducing burdens on the most compliant businesses, for example by exploring the scope to set appropriate thresholds for notification, to introduce exemptions where other existing requirements to notify are in place, and to develop an easy mechanism for notification where this is required.

**Recommendation 13:** *The relationship between a business and its customer compliance manager appears to be key to HMRC's success in managing large business tax risk. We are concerned to hear that this may be under strain. We recommend that the Government identifies what steps can be taken to support existing customer compliance managers and to expand the number of companies benefiting from a customer compliance manager relationship. If this proposal goes ahead, the Government should commit to ensuring that every business affected has a customer compliance manager. (Paragraph 162)*

**The Government partially accepts this recommendation.**

HMRC's Large Business directorate works with around 2,000 of the UK's largest and most complex businesses to make sure they pay the correct amount of tax at the right time. HMRC assign a senior professional called a Customer Compliance Manager (CCM) to each of the UK's largest businesses. Their primary role is to make sure the business pays everything it owes. CCMs are experts in their field and build an in-depth knowledge of the business and the sectors it operates in. They are also supported by tax specialists for all regimes, and can call on data analysts, solicitors, audit specialists, trade sector experts and forensic accountants.

HMRC engage with large businesses to gather feedback on their taxpayer experience and have no information that the relationship between business and customer compliance managers is under strain. The tax gap for large businesses in 2018-19 was £5.3bn, having decreased from £7.65 bn in 2005-06.

Under HMRC's current proposals, there are a small number of businesses that will fall into the proposed regime who do not have a CCM. In the planned further consultation on this measure, the Government will explore what additional support these businesses might need in order to meet their new obligations.

## 6. New tax checks on licence renewal applications

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***Recommendation 14:** Before 400,000 businesses are required to undergo a tax check, we would have expected HMRC to publish an analysis of tax compliance in the relevant sectors to support the decision to apply conditionality first to them. In line with the policy principles set out earlier in our report, more information is needed to support the application of tax checks in these circumstances. (Paragraph 174)*

*Therefore, before the tax check legislation is introduced in Parliament, the Government should publish an analysis of compliance in the sectors affected, to demonstrate that the problem of hidden economy activity is such that the tax check proposed is a proportionate response. (Paragraph 175)*

### **The Government does not accept this recommendation.**

The Government recognises and agrees with the principle that policy measures - and the underlying problems that they are aimed at - must be clearly explained, including through appropriate consultation. This aligns with the Government's commitment to how to develop tax policy changes.

The Government has set out, during consultation and subsequently, the purpose of conditionality: it is intended to divert taxpayers away from the hidden economy as early as possible within a business's lifecycle. It has also explained the factors that have guided the decision to apply the tax check within these sectors – specifically, the Government has weighed an assessment of risk posed by the hidden economy against an assessment of the suitability of licensing rules to accommodate a tax check (for example, where licence holders are already required to demonstrate that they are 'fit and proper').

The Government has also published its assessments of benefits associated with the policy, based on the anticipated impact of bringing people out of the hidden economy, alongside the anticipated administrative costs to businesses. This assessment of benefits has been certified by the Office of Budget Responsibility (OBR) and will be fully evaluated.

The Government has taken extensive views from stakeholders before reaching a decision, the majority of whom have supported the principle of applying tax checks to licensing, provided that any administrative burden is minimised. Representative groups such as the Local Government Association and trade representatives have been actively involved in this process. This engagement has taken place during consultation and during the development of draft legislation, and the process of gathering insight and feedback from individuals in the sectors continues. Taxpayer representatives have suggested this could be a valuable tool in tackling non-compliance, licensing body representatives have suggested the checks can be incorporated into licensing relatively simply, and some representative groups have said they welcome the check as a way of supporting compliance in the relevant sectors.

HMRC will ensure, through guidance and stakeholder engagement, that the aims of the policy and the case for applying it within the sectors concerned, are clearly explained. As part of that,

HMRC will continue to explore opportunities for new and innovative communications approaches to help ensure taxpayers are aware of and understand their obligations, including harder to reach groups.

***Recommendation 15:** We recommend that the tax check is limited to confirming that the applicant is registered for tax and has a unique tax reference (UTR). This is the basis on which consultation has been conducted, and we are not persuaded that the case for going further has been made. (Paragraph 186)*

**The Government does not accept this recommendation.**

The Government has noted the Committee’s concerns and recognises the need to ensure that tax legislation is consistent with the approach taken to consultation. However, the Government does not agree that the tax check exceeds the policy approach set out during consultation, which focused on ensuring that a person is ‘appropriately registered for tax’. In response to the consultation, the Government stated – in accordance with feedback from stakeholders – that the best way to achieve this aim would be to develop a digital service allowing an applicant to demonstrate their tax registration status.

The draft legislation allows HMRC to test compliance with the legal obligation to notify chargeability to income tax or corporation tax (this is how the legislation reflects the concept of ‘tax registration’). Those obligations are specific to each tax year (for income tax purposes) or accounting period (for corporation tax purposes). By contrast, a Unique Tax Reference Number (UTR) is issued once and does not confirm that these legal obligations have been – or continue to be – met. The Government has decided that collecting a UTR would not, in itself, be a suitable way to test compliance with the legal obligation to notify chargeability to income tax or corporation tax.

The draft legislation will also allow HMRC to ask applicants to declare whether they have reported their income from the licensed activity on their tax return. This is to address the risk that they may be registered for tax in respect of another activity, but not disclosing their licensed income – “moonlighting”.

The tax check would not extend beyond this. For example, it would not involve HMRC asking how much income has been reported or whether it has been reported accurately. This ensures that the scope of the tax check is limited to ensuring that businesses are not hidden from HMRC, and it is the Government’s view that this is consistent with the aim, set out in consultation: to ensure that a person is appropriately registered for tax.

*Recommendation 16: Paragraph 5(1)(b) of the draft Schedule in the legislation should be amended to define more tightly the information which can be required of applicants for licence renewals. (Paragraph 189)*

### **The Government accepts this recommendation**

The Government agrees to amend the draft schedule to make clearer the information that can be required as part of the tax check. This will be in accordance with the explanation of the scope of the tax check set out in the response to the previous recommendation.

However, the Government considers that amending Paragraph 5(1)(b) of the draft schedule may not be the best way to achieve this aim. The Government will bring forward amendments to the draft schedule which will make clearer the information that can be required for the tax check.

**Recommendation 17:** *Conditionality is an unproven policy. It remains to be seen whether it will achieve the Government's objectives for it. The Government should proceed cautiously.*

We

recommend:

- *Before conditionality is applied to other sectors, the effectiveness of the legislation in the private hire vehicle, taxi and scrap metal sectors should be evaluated. This evaluation should look separately at the educational and information element relating to applicants for new licences, and at the impact of the tax checks, in particular whether it has led to unintended consequences, such as an increase in unlicensed operations;*
- *The application of conditionality to other sectors should be justified by reference to a specific problem in the relevant sector; and*
- *Before introducing tax checks, HMRC should work with stakeholders to communicate clearly to applicants for licences what the tax check is for and what it consists of, bearing in mind the diversity of the sector and the need to cater for those who cannot be reached using digital methods and for whom English is not their first language. (Paragraph 194)*

### **The Government partially accepts this recommendation.**

The Government agrees the need for thorough consultation on new forms of tax conditionality, reflecting the careful and iterative approach to development of this legislation.

The Government also agrees the need to evaluate this legislation and has made specific provision to evaluate the effectiveness of the tax check (paragraph 5(1)(b) of the draft schedule). The Government agrees the importance of ensuring that the tax check does not discourage people from renewing a licence and has taken extensive steps – including through consultation – to ensure that the tax check is minimal in nature. HMRC will work with other Government departments and licensing bodies to monitor and mitigate any unintended consequences.

The Government will consider further the extent to which the obligation set out at paragraph 2 of the draft schedule (applying when licensing bodies are dealing with first-time applications) would form part of the evaluation of this policy.

However, the Government does not agree that this evaluation must be completed before any potential wider approaches are developed. The Government agrees with the views of stakeholders that conditionality – making the provision of approvals or services conditional on good tax compliance – offers another important tool for HMRC as they aim to ensure a level playing field for all taxpayers. There are a range of ways in which conditionality could be applied to address tax non-compliance. These could further address the hidden economy tax gap – which is estimated to be £2.6bn in tax year 2018 to 2019 – or wider behavioural segments of the tax gap. The Government will continue to explore these options; and any further forms of conditionality would be subject to appropriate consultation.

The Government also agrees that HMRC should work with stakeholders to communicate the purpose and requirements of the tax check before it is introduced. This will be carried out through provision of guidance, wider communications and continued engagement with stakeholder groups. The Government has made clear that it will address the particular needs of anyone who holds protected characteristics, in particular, through the provision of appropriate support and guidance. It will also ensure that individuals who may be digitally excluded or need extra support are directed to additional help, via established HMRC processes.

More broadly, in line with the commitment made in the recent HMRC evaluation of powers report, HMRC will continue to explore opportunities for new and innovative communications approaches to help ensure that taxpayers, including harder to reach groups, understand their obligations.

## 7. Cross-cutting themes

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***Recommendation 18:** When proposing new or extended powers for HMRC, the Government should specifically explain why existing powers are insufficient to achieve the policy objective. This was done in the case of the promoters legislation where the problems with the current legislation were explored in the consultative document, along with the impact this was having on HMRC's ability to defeat promoters' activities in a timely way. (Paragraph 198)*

*We also recommend that the Government adopts a standard practice of providing detailed analysis to justify any new proposal conferring new or extended powers on HMRC. (Paragraph 199)*

### **The Government accepts this recommendation.**

The Government is committed to early and continuing engagement on tax changes and to exploring new ways of broadening public engagement with development of the tax system.

The Government already has a standard practice of providing detailed analysis to explain the purpose of any new proposals, via the publication of tax information and impact notes (TIINs) for tax policy changes. HMRC and HM Treasury have made an undertaking to publish TIINs for all substantive tax and National Insurance policy changes; this was announced by a Written Ministerial Statement to Parliament on 15 March 2011. TIINs already give a clear explanation of the policy objective and why the measure is necessary to tackle a mischief or threat to revenues.

The TIIN combines the Budget note and impact assessment in one easy-to-read format and was one of the improvements brought in as part of the "new approach" to tax policy making in 2010. The TIIN sets out very clearly what change is being proposed, why it is being introduced and the reason for any change being made.

TIINs also give a clear explanation of the policy objective together with details of the tax impact on:

- the Exchequer
- the economy
- individuals
- businesses
- civil society organisations
- any equality or other specific area of impact

The Government will consider further the extent to which a detailed analysis is included in HMRC consultation documents which confer new or extend powers on HMRC.

***Recommendation 19:** In line with the principles we set out in Chapter 2, tax legislation should be targeted on the taxpayers it is intended to affect. We recommend that consulting with stakeholders about how action can best be targeted is made a standard feature of all calls for evidence and consultations. (Paragraph 221)*

### **The Government accepts this recommendation.**

The Government recognises the importance of engaging fully with individuals, practitioners, businesses and other organisations in the development of tax policy. In 2010 the Government set out improvements to the tax policy making process including a published tax consultation framework, which was updated in 2017. As set out in that framework, the best public engagement allows the Government to explore, develop and test new ideas to improve the tax system and ensure that change is well targeted, and impacts are well understood.

The Government is and remains committed to the tax policy making approach in the development of policy changes. This has resulted in the majority of tax policy changes being subject to consultation both on the policy and draft legislation, ensuring that the policy and legislation are effective. For example, as a result of listening to stakeholders, the Government extended the consultation deadlines for several tax policy documents announced at the Budget in early 2020. In order to meet Government commitments on enabling technical consultation of draft legislation, two separate 'L-days' were held; one in July 2020 and a further one in November 2020. Furthermore, where consultations are carried out, response documents are subsequently published as a matter of course.

The Government continues to seek opportunities to find how the consultation approach can be more effective and how engagement can provide greater insight to the effects of a policy change. HMRC's guidance will be updated to further emphasise the importance of targeting tax legislation on the taxpayers it is intended to affect.

*Recommendation 20: We recommend that, for any future proposal involving outsourcing, the Government specifically explains why HMRC is not carrying out the function itself, and what the justification for outsourcing is. (Paragraph 236)*

**The Government accepts this recommendation.**

It can be more proportionate and effective to design tax policy so that trusted third parties are involved in supporting taxpayers, including carrying out suitable activities to make tax easy to get right and difficult to get wrong.

The Government's published strategy - Building a Trusted, Modern Tax Administration System published in July 2020 - is clear that HMRC aim to work more closely with those who have a closer relationship with the taxpayer than a statutory authority ever could, and hold data and insight that HMRC do not routinely acquire.

Working with third parties, such as employers and other intermediaries, accountants and tax agents, software developers and data providers, is an important part of HMRC's strategic approach. The Government recognise that these organisations play an important role in supporting tax compliance, however HMRC are always mindful of the burden that this places on them and are careful to design new policies and processes to minimise this.

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<sup>i</sup> <https://www.gov.uk/government/publications/evaluation-of-hmrcs-implementation-of-powers-obligations-and-safeguards>