

TAXREP 22/08

PAYMENTS, REPAYMENTS AND DEBT

Comments submitted on 11 March 2008 by the Tax Faculty of the Institute of Chartered Accountants in England & Wales to HM Revenue & Customs in response to the consultation document 'Modernising Powers, Deterrents and Safeguards: Payments, Repayments and Debt' issued on 10 January 2008.

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Chartered Accountants' Hall PO Box 433 Moorgate Place London EC2P 2BJ www.icaew.com	T +44 (0)20 7920 8646 F +44 (0)20 7920 8780 DX DX 877 London/City
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PAYMENTS, REPAYMENTS AND DEBT

INTRODUCTION

1. In this document we present the comments of the Tax Faculty of the Institute of Chartered Accountants in England and Wales (ICAEW) on the consultation document *Modernising Powers, Deterrents and Safeguards: Payments, Repayments and Debt* (the Condoc) issued by HM Revenue & Customs (HMRC) on 10 January 2008.
2. We are pleased to have the opportunity to respond to this consultation. We would be happy to discuss any aspect of our comments and to take part in all further consultations on this area.
3. Information about the Tax Faculty and the ICAEW is given in Annex A. We have also set out, in Annex B, the Tax Faculty's ten tenets for a better tax system, by which we benchmark proposals to change the tax system.

KEY POINTS SUMMARY

4. Our key comments on this consultation are as follows:
 - We are very concerned that the draft legislation leaves a great deal to regulations, particularly as draft regulations have not been published so that it is not possible to understand fully the effect of the proposed legislation.
 - We strongly believe that if statutory powers are to be subject to limits or conditions, then these safeguards should also be spelled out in statute. There are a number of safeguards mentioned in the Condoc which should be in the draft legislation but which are not. There are also a number of necessary safeguards which are not mentioned in the Condoc at all.
 - We are in favour of aligning the powers for distraint and for court enforcement procedures.
 - However, we are concerned because it is not clear what protections the taxpayer will have against the use of Sch 12, TCA 2007 (which deals with taking control of goods) by HMRC. Particular issues are: what goods will be exempt? How long will goods be held before they are sold? And will HMRC have power to enter without a warrant?
 - We are also concerned at the proposal to extend HMRC's right to proceed against goods to amounts due under a contract settlement. We believe that HMRC ought to rely on contract law to enforce contracts in the same way as other parties to a contract.
 - We support the principle of offsetting amounts due to and from HMRC by the same person.
 - However, we do not agree that offsetting should extend to related parties. This can in effect reinstate crown preference. The offsetting legislation should

not extend to related parties until there has been an opportunity for proper public consultation on whatever is proposed.

- We are concerned that set-off is to be entirely within HMRC's power and exercisable at its discretion. Until HMRC can demonstrate that its systems are able to produce reliable, accurate assessments of taxpayer's liabilities on a consistent basis, we cannot support a regime where the power to make a set-off rest entirely with HMRC and the taxpayer has no legal right to object
- We believe that there should be a right of appeal against HMRC's decision to offset tax debits and credits.
- HMRC should be required by law to offset debits and credits in whatever way is most favourable for the taxpayer.
- We are pleased to see that HMRC does not intend to disturb the principles for offsetting debts in insolvency. This should be made clear in the proposed tax legislation, b
- Tax credits should be left entirely outside these offsetting rules, and the legislation should make this clear. We do not agree that HMRC should be able to use a tax repayment to reduce a tax credit overpayment.
- The ability to pay by credit card will be a useful option for many of our members' clients.
- HMRC should not be empowered to pass on transaction costs of credit card payment in excess of the costs it is itself charged by the third party provider.
- Collecting small debts via PAYE could be a useful option for many taxpayers.
- We would prefer that this is done only with the taxpayer's consent rather than with HMRC's compulsion.
- Since the Condoc contains very little detail of this proposal and no legislation, it should be deferred until the detailed proposals have been published and properly consulted upon.

ADEQUACY OF PROTECTION FOR THE TAXPAYER

5. Before commenting on the detailed proposals, we have some general comments about the protections for the taxpayer, or lack of them, in this consultation.
6. We are very concerned that the draft legislation leaves a great deal to regulations, particularly as draft regulations have not been published so that it is not possible to understand fully the effect of the proposed legislation. We think it unreasonable that it should be left to HMRC to determine in what circumstances the State can deprive a citizen of his assets. That ought to be a matter solely for Parliament to determine. We also think it important that a taxpayer should be able easily to understand his rights and relegating safeguards and detailed provisions to secondary legislation will make it difficult for a person to do so.

7. We strongly believe that if statutory powers are to be subject to limits or conditions, then these safeguards should also be spelled out in statute. We are concerned by the increasing tendency for HMRC to seek broad and wide-ranging statutory powers, with the limits on their use set out in non-statutory guidance.
8. The reasons why providing safeguards in guidance alone is inadequate are:
 - Guidance can be changed or withdrawn.
 - Taxpayers (especially the unrepresented) may not be aware of its existence.
 - HMRC staff may not apply it appropriately.
 - The courts cannot consider it – they will look only at the widely-drawn legislation – which leaves taxpayers little remedy apart from making a formal complaint or seeking judicial review (which is unrealistic for most taxpayers).
 - It does not receive Parliamentary scrutiny.
9. We have identified a number of safeguards in this response which we think should be in statute but which are not in the draft legislation.
10. A different type of safeguard is the opportunity for adequate and effective public consultation. In this context it is disappointing that details of some of these proposals are not available for comment now, and appear to be work in progress. For example, the rules on related entities; details of what the operational guidance on offsetting will contain; details of the fees which would be charged for credit card payments; and most of the detail on collecting debts via PAYE.

REMOVING INCONSISTENCIES IN ENFORCEMENT POWERS

11. We are in favour of aligning the powers for distraint and for court enforcement procedures, so that HMRC can take one action for several different tax debts owed by the same taxpayer. We can see that this could lead to lower costs and less disruption for the taxpayer, as well as saving HMRC's resources.
12. In the draft legislation, the intention appears to be that s 61, TMA 1970 will in future only apply to Northern Ireland. In England and Wales, enforcement of tax debts by taking control of goods will be governed by Sch 12, Tribunals, Courts and Enforcement Act 2007 (TCE 2007).
13. We are concerned by this because it is not clear what protections the taxpayer will have against the use of Sch 12, TCA 2007 by HMRC. Schedule 12 provides for goods to be taken unless they are exempt, and the exemptions are to be specified by regulation. As far as we are aware, these regulations are not yet available. At the moment HMRC follows a practice of not distraining certain goods, such as those which are jointly owned or which are essential tools of the taxpayer's trade. We should like reassurances – and preferably evidence in the shape of draft regulations – that the existing safeguards for the taxpayer which HMRC observes in distraint proceedings will be preserved.
14. Section 61(3), TMA 1970 requires HMRC to keep the goods seized for five days before selling them. This should be preserved in any new rules. Para 39, Sch 12, TCE 2007 provides for a minimum period, to be specified by regulation – we do not yet know what that will be.

15. Under the present legislation, HMRC has power to distrain, but cannot insist on entry to premises in order to distrain goods unless it obtains a court warrant (s 61(2), TMA 1970). Under para 14, Sch 12, TCE 2007, an enforcement agent 'may' enter relevant premises without a warrant. This appears to give HMRC wider powers than at present. We think that the current requirement to obtain a warrant before insisting on entry should be preserved.
16. We are also concerned at the proposal in section 1(1) of the draft legislation to extend HMRC's right to proceed against goods to amounts due under a contract settlement. There is no such right under current law and HMRC has not indicated why it believes that powers which apply to tax should be extended to purely civil debts. We believe that HMRC ought to rely on contract law to enforce contracts in the same way as other parties to a contract. We also believe that the definition of a contract settlement could give rise to arguments. For example, a taxpayer sometimes includes in an offer liabilities that are out of time for assessment and we doubt that such an amount can be said to be 'in connection with any person's liabilities'. An offer is also sometimes made as a pragmatic way to resolve a dispute albeit that the taxpayer does not believe that any tax is due. We also doubt that such an offer is in connection with a liability. We do not think that taking goods is an appropriate remedy where there is a possibility of a dispute.
17. We do not understand what is meant in new section 1(7) by 'transitional provision and savings' (which the section says may be made by order when the new legislation is brought into force). We should like clarification of what this means, and in particular, of what transitional provisions HMRC has in mind.

SETTING OFF REPAYMENTS AND DEBTS

18. We support the principle of offsetting amounts due to and from HMRC by the same person. This could be practical and convenient for the taxpayer, as well as an effective recovery tool for HMRC. However, we do not agree that offsetting should extend to related parties – see paragraph 32 below.
19. However, we are concerned that set-off is to be entirely within HMRC's power and exercisable at its discretion. There are inadequate safeguards for the taxpayer because:
 - There is no right of appeal against HMRC's decision.
 - The taxpayer does not have the right to opt for set-off himself.
 - There are wide powers in the draft legislation, and few safeguards.
 - Safeguards solely in the form of HMRC's operational guidance are not adequate.

Safeguards

20. There is very little mention of safeguards in the Condoc. Para 2.13 says that set-off will be done only for 'established debts' and para 2.14 says that HMRC will have 'clear operational criteria for when ... set-offs would take place'. We discuss both of these below.
21. We believe that there should be a right of appeal against all decisions made by HMRC, and therefore that the taxpayer should be able to appeal against HMRC's decision to set off debts and repayments.

22. Offsetting should not be used for liabilities which are under appeal, or which are the subject of a formal complaint which is being investigated.
23. The order of offset may make a big difference to taxpayers in terms of interest, surcharges, etc. There is nothing in the legislation or the Condoc about how HMRC will deal with this. HMRC should be required to offset debits and credits in whatever way is most favourable for the taxpayer. This safeguard should be in legislation.
24. Taxpayers should be told in advance of HMRC's decision to offset debits and credits (as noted at para 3.19 in the notes to the legislation. This safeguard should be in legislation. HMRC also needs to explain clearly when and how the offset will be done.
25. The Condoc mentions two specific safeguards – in respect of tax credits and assignments to charities (see below) – but these are not in the legislation. They should be in legislation and not left to HMRC's operational guidance.

Established debts

26. The Condoc emphasises that set-off will only be used for 'established' debts where HMRC could take action for sums it is owed. The implication is that an established debt is a correct debt. However, this is not necessarily the case. Our members can provide many examples of tax assessments or penalty determinations being incorrect due to HMRC error. Taxpayers without good representation may not realise there is an error, or may be ill-equipped to dispute it. Therefore, the debt would be 'established' as defined in section 3(3) of the draft legislation, because it would be payable 'under or by virtue of an enactment'.
27. Until HMRC can demonstrate that its systems are able to produce reliable, accurate assessments of taxpayer's liabilities on a consistent basis, we cannot support a regime where the power to make a set-off rest entirely with HMRC and the taxpayer has no legal right to object.

HMRC operational guidance

28. As noted at paragraph 7 above, we strongly believe that if statutory powers are to be subject to limits or conditions, then these safeguards should also be spelled out in statute.
29. Further, apart from the vague statement that HMRC will have 'clear operational criteria for when ... set-offs would take place', the Condoc gives no indication of what these criteria might be or what safeguards they might contain. We consider this to be highly unsatisfactory.
30. As in the case of 'established debts', we are not confident of HMRC's ability to consistently get it right in operating its guidance. Will HMRC staff be able to identify cases where offsetting would not be appropriate, eg where it might cause hardship or business failure?

Related entities

31. The legislation does not attempt to define 'related entity' and the Condoc indicates that this area is work in progress. There are many important issues to be

considered here – for example, the implications for groups of companies, VAT groups, partners in partnerships, joint claims for tax credits. We strongly recommend that the offsetting legislation is not extended to include related parties until there has been an opportunity for proper public consultation on whatever is proposed.

32. We do not think it appropriate to extend the power to make offsets to debts due from related persons. This can in effect reinstate crown preference, which was specifically abolished by Parliament, by enabling HMRC to obtain payment of its debt from an insolvent company by offsetting the debt against an amount due to a related person. Not only would that undermine the will of Parliament but it creates unfairness to other creditors if HMRC has power to appropriate assets of A against debts of B thus prejudicing the creditors of A.

Assignments of debt

33. The Condoc says at para 2.17 that if a taxpayer has assigned an overpayment to charity via the self assessment system, HMRC 'will honour the assignment'. This is not in the legislation. It should be in statute and not left to HMRC's operational guidance.
34. We feel that HMRC should respect assignments to professional advisers except where the taxpayer or the adviser has been given notice of the intention to offset prior to the assignment. It is not uncommon for both accountants and lawyers to assist a taxpayer on the basis that they will be paid out of the tax repayment. This is in the interests of justice as it enables a taxpayer to obtain representation to protect his or her rights where representation might not otherwise have been obtainable. Advisers are likely to be reluctant to continue to act on this basis in future if there is a risk that the anticipated repayment will be diverted to pay tax debts that may not even have been due at the time of the assignment.

Insolvency

35. We note the reference to insolvency at para 3.24 in the notes to the draft legislation. We are pleased to see that HMRC does not intend to disturb the principles for offsetting debts in this situation. This should be made clear in the proposed tax legislation, by stating something on the lines of: 'This section shall not apply when the person is subject to an insolvency process under the Insolvency Act 1986 (as amended), where the insolvency rules shall prevail.'
36. Para 3.24 in the notes to the draft legislation says that HMRC will consult further with interested parties on this issue. We should like to participate in this consultation.

Tax credits

37. Tax credits is a particular area of concern.
38. The Condoc specifically says (para 2.16) that tax credits will not be used to reduce a tax debt. We entirely agree with this. It is not, however, specifically stated in the legislation.
39. We assume that child benefit will be treated similarly but would like confirmation of that. Again, if it is to be left outside offsetting, this should be in statute.

40. We are strongly of the view that tax credit overpayments should be completely left out of the offsetting arrangements. We do not agree that HMRC should be able to use a tax repayment to reduce a tax credit overpayment.
41. Many of those struggling with tax credit overpayments are likely to be on low incomes, and offsetting an anticipated tax refund (which might be needed to pay for essential living expenses) against a tax credit overpayment could create financial hardship. We are not convinced of HMRC's ability to identify such cases of potential hardship, and therefore it would be safest to leave tax credits out of offsetting altogether.
42. We foresee difficulties in identifying an 'established' debt for tax credit purposes. There is still a high level of overpayments due to HMRC error, and some overpayments may be under dispute – although not necessarily under appeal, as there is no right of appeal against a decision to recover an overpayment. Would a disputed overpayment be treated as an established debt?
43. Offsetting could only (we assume) be used against a tax credit overpayment which is being recovered by direct collection. This will only apply where the award has ended and there is no ongoing entitlement from which the overpayment can be recovered. So a claimant whose overpayment is being recovered directly could have it offset with a tax refund due to him; whereas a claimant owing the same amount of tax credits, but with an ongoing award, would get the full tax refund while continuing to repay his tax credits over time. This is unfair to those claimants who, because of the way the tax credits system happens to work, have an overpayment which is subject to direct collection.
44. HMRC's stated practice is that claimants can, if they choose, pay off tax credit overpayments in 12 monthly instalments. They do not need to give a reason and there is no interest. The offsetting legislation, as drafted, would allow HMRC to override this practice.
45. A tax credit overpayment from a joint claim is a joint and several liability of the couple (or former couple). This introduces further complications. HMRC's stated approach is, as a starting point, to seek 50% of the debt from each partner. Would HMRC seek to over-ride this if one of the partners was due a tax refund?

Agents

46. Where the taxpayer has an appointed agent, HMRC should contact the agent in the first instance regarding offsetting and how it is to be done.

ACCEPTING PAYMENT BY CREDIT CARD

47. The ability to pay by credit card will be a useful option for many of our members' clients. We assume that the proposal in the 2007 consultation document to offer credit card payment only for overdue amounts has been dropped, and that this payment option will be available to all taxpayers.
48. It is disappointing that the Condoc gives no indication of what fee might be charged.

49. HMRC should not be empowered to pass on transaction costs in excess of the costs it is itself charged by the third party provider.
50. Taxpayers who are already in financial difficulty will be at risk of adding to their difficulties if they can pay by credit card. We are pleased to note the safeguards listed at para 2.22. However, the success of these in protecting vulnerable taxpayers will depend on HMRC guidance and how it is operated. In our experience, HMRC has only qualified success in identifying those who cannot pay and treating them appropriately.

COLLECTING SMALL DEBTS THROUGH PAYE

51. This proposal could be a useful option for many taxpayers.
52. However, we would prefer that this is done only with the taxpayer's consent rather than with HMRC's compulsion. We are pleased to note the taxpayer would have a right of appeal.
53. It is difficult to comment on it at this stage, as the Condoc contains very little detail and no legislation. Although this is one of the four proposals which HMRC has developed and plans to take forward, it is clear that there is a lot more work to be done.
54. In view of this we strongly recommend that this proposal should not be included in this year's Finance Bill but should be deferred until the detailed proposals have been published and properly consulted upon.

JMM
11 March 2008

ANNEX A

THE ICAEW AND THE TAX FACULTY: WHO WE ARE

1. The Institute of Chartered Accountants in England and Wales (ICAEW) is the largest accountancy body in Europe, with more than 128,000 members. Three thousand new members qualify each year. The prestigious qualifications offered by the Institute are recognised around the world and allow members to call themselves Chartered Accountants and to use the designatory letters ACA or FCA.
2. The Institute operates under a Royal Charter, working in the public interest. It is regulated by the Department for Business, Enterprise and Regulatory Reform through the Financial Reporting Council. Its primary objectives are to educate and train Chartered Accountants, to maintain high standards for professional conduct among members, to provide services to its members and students, and to advance the theory and practice of accountancy, including taxation.
3. The Tax Faculty is the focus for tax within the Institute. It is responsible for tax representations on behalf of the Institute as a whole and it also provides various tax services including the monthly newsletter TAXline to more than 11,000 members of the ICAEW who pay an additional subscription.
4. To find out more about the Tax Faculty and ICAEW including how to become a member, please call us on +44 (0)20 7920 8646 or email us at taxfac@icaew.com or write to us at Chartered Accountants' Hall, PO Box 433, Moorgate Place, London EC2P 2BJ.

ANNEX B

THE TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. **Statutory:** tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. **Certain:** in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. **Simple:** the tax rules should aim to be simple, understandable and clear in their objectives.
4. **Easy to collect and to calculate:** a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. **Properly targeted:** when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. **Constant:** Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. **Subject to proper consultation:** other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. **Regularly reviewed:** the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. **Fair and reasonable:** the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. **Competitive:** tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see <http://www.icaew.com/index.cfm?route=128518>).