



CONTRACTUAL DISCLOSURE FACILITY

Comments submitted in October 2011 by the Tax Faculty of the Institute of Chartered Accountants in England & Wales to HM Revenue & Customs in response to the consultation document *Civil Investigation of Fraud – Contractual Disclosure Facility* issued on 20 July 2011.

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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 *Civil Investigation of Fraud – Contractual Disclosure Facility* (the condoc) issued by HM Revenue & Customs (HMRC) on 20 July 2011.
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. We have already provided oral feedback to HMRC at a meeting of our Tax Investigation Practitioners Committee on 8 September 2011.
3. Information about the Tax Faculty and the ICAEW is given below. We have also set out, in Appendix 1, the Tax Faculty's ten tenets for a better tax system, by which we benchmark proposals to change the tax system.

WHO WE ARE

4. ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter which obliges us to work in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 136,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.
5. In the region of 43,000 ICAEW individual members are in practice. 12,000 firms, ranging from the 'Big 4' to sole practitioners, are authorised by ICAEW to practice.
6. ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.
7. The Tax Faculty is the voice of tax within ICAEW and is a leading authority on taxation. Internationally recognised as a source of expertise, the faculty is responsible for submissions to tax authorities on behalf of ICAEW as a whole. It also provides a range of tax services, including *TAXline*, a monthly journal sent to more than 8,000 members, a referral scheme and a weekly tax newswire sent to over 18,000 registered users.

KEY POINTS SUMMARY

8. Broadly speaking we agree with the policy objectives and support the proposal in the condoc. We do have some concerns and comments as set out below. In particular:
 - We do not think that a standard 60 day period is sufficient for responding to the contractual disclosure facility (CDF) offer and providing the outline disclosure (OD). Our recommendations are that there should be longer standard period, or alternatively a period in which to accept the CDF offer and then a further period in which to complete the OD.
 - We should like to see HMRC's legal advice that CDF can only be used for fraud and that it is not possible to amend the current COP9 procedure to withdraw protection from prosecution if the taxpayer ceases to cooperate.
 - We are concerned about those taxpayers who are unwilling to admit fraud but willing to cooperate. We should want to see a strong undertaking from HMRC that officers will

respect that cooperation, explain the concerns and seek to move matters on collaboratively.

- Good case selection is crucial, so that the CDF is offered only where there is good evidence of fraudulent activity.
- HMRC should not make the requirements of the OD too detailed or time-consuming to prepare.
- HMRC should make clear the minimum requirements of the CD.
- Code of Practice 9 will need to be re-written to make it clearer and more effective.

RESPONSES TO SPECIFIC QUESTIONS

Question 1. Do you agree the operational policy objective?

9. Yes, broadly speaking we agree with the policy objectives as set out at para 1.13 of the condoc. The civil investigation of fraud process does need more 'teeth' to make taxpayers aware of the consequences of non-cooperation and of failure to make full disclosure, while encouraging cooperation. We have previously made this point in meetings between our Tax Investigation Practitioners Group and HMRC.
10. We also support in principle the objective at para 1.14 of reducing the time taken to work a case. However, a tight timetable should not impose unnecessary burdens on the taxpayer or mean that through lack of time the disclosure is inaccurate or incomplete. As discussed below, we think that the 60 day initial period is too short and we are not convinced that the CDF will reduce the time to conclude a case compared to the current CIF procedure.

Question 2. Is sixty days reasonable for the taxpayer to talk to their advisors and make an outline disclosure of their tax irregularities?

11. There are three issues here: the delivery of HMRC's CDF offer, obtaining the information to make an OD and the role of the adviser.
12. **Delivery of the CDF offer:** We have commented on problems with HMRC's post-handling in other submissions to HMRC. Relevant here is the delay which can occur between the HMRC officer originating a letter and the letter arriving with the taxpayer. Clearly delays at this stage could eat into the 60 days allowed for a response.
13. We suggest that the 60 days should run from the date the taxpayer receives the CDF offer. Alternatively, if the 60 days is to run from the date of the offer letter, HMRC must ensure that the letter arrives promptly.
14. **Information needed for an OD:** Whether 60 days is sufficient will depend on what is envisaged by an OD: how much detail is required and how precisely the fraud must be quantified. We discuss the OD below, under 'Other comments on the proposals'.
15. It appears that the OD will be quite a detailed document and that, crucially, it must contain details of each fraud. On this basis, 60 days will be too short in many cases, for example where the taxpayer will not be able to indicate the amounts involved with any precision without obtaining copy bank statements, perhaps going back many years. It is well known that the initial response of most banks to such a request is to say that they cannot go back more than six years, and it can easily take 60 days to obtain copy statements.
16. Similarly if an overseas company or overseas trust is involved it can be difficult to obtain information, particularly if there has been a change of trustee or manager during the period involved. 60 days is normally inadequate for this.
17. The need to identify each fraud poses an additional problem. Under the current procedure, as the work on a taxpayer's affairs progresses and information is collected, it is not unusual

for new issues to emerge in addition to the irregularities which originally prompted the investigation. 60 days may be insufficient to make sure that all frauds have been identified; and clearly this is crucial for the taxpayer, because if any frauds are missed they will not be covered by the protection the CDF is to provide.

18. **The role of the adviser:** If the recipient of a CDF offer is unrepresented, he or she will need to engage a suitable adviser. Even if the taxpayer is represented, the existing agent may not be equipped to deal with this sort of case and will prefer to bring in a specialist adviser. Given the importance of the taxpayer – and the adviser – understanding what is meant by fraud, specialist advice will usually be necessary. The taxpayer will need to take reasonable care in engaging an adviser and this may take time; quite possibly, it would take up the first two or three weeks after the taxpayer receives the CDF offer.
19. In conclusion, we do not consider that a standard period of 60 days is long enough for the taxpayer to respond to HMRC with the OD. It may be sufficient in some cases, especially simpler ones involving small amounts, but not in others. We suggest that the standard period should be longer – perhaps 90 days. Alternatively the taxpayer should have 60 days to respond to the CDF offer and accept it in principle, and then a further period within which to complete and submit the OD. HMRC should also exercise discretion to allow a longer period than the standard one in which to submit the OD, if this makes sense in the circumstances of a particular case.

Question 3. Do you think that there are benefits to the contractual disclosure facility and do you think the proposed structure is reasonable?

20. We accept that the CDF offers benefits for cases involving fraud. Broadly we agree with the proposed structure, subject to comments on specific aspects of it, as set out elsewhere in this TAXREP.
21. The CDF is to be limited to cases of fraud. We have concerns about two categories of people.
22. Firstly, those who may feel obliged to accept the CDF offer and admit fraud in order to obtain protection from prosecution, even if they do not think their actions have been fraudulent, because they are worried that HMRC might take a different view.
23. Secondly, those people who are reluctant to admit to fraud up-front but are willing to come forward, make full disclosure and clear their name with the protection that CIF or CDF offers. The word 'fraud' often conjures up visions of imprisonment, and to require a taxpayer to admit to fraud up-front has to overcome a psychological barrier. Admitting to 'irregularities' without considering whether or not they are fraudulent is far easier for taxpayers than admitting to fraud.
24. We understand that HMRC has legal advice to the effect that the CDF must only be used in cases of fraud, and that it is not possible to amend the current COP9 procedure so that protection from prosecution is withdrawn if the person fails to cooperate. This would prevent an adjustment to the existing CIF procedure, and the possibility of making the CDF terms available to those who are willing to admit to irregularities rather than fraud up-front: both of these being suggestions we would have made to address the issues of the two categories of taxpayer we have mentioned above.
25. HMRC does not generally publish legal advice it has obtained, but in this instance it would be very helpful to see the advice in question.
26. The first category – those who do not think they have committed fraud but feel obliged to admit to it in order to have protection from prosecuting – underlines the importance of HMRC

selecting the right cases so that the offer of the CDF is limited to those cases where there is really good evidence of fraud. We discuss case selection further below.

27. Where a person is offered the CDF but does not want to admit to fraud, there are two options: HMRC undertakes its own investigation with taxpayer cooperation: or HMRC starts its own investigation, on its own.
28. Where the taxpayer is unwilling to admit fraud but willing to cooperate, we should want to see a strong undertaking from HMRC that officers will respect that cooperation and seek to move matters on collaboratively rather than behind closed doors. We think this situation falls within the new LSS which undertakes that, in dispute cases, HMRC will articulate its concerns and give the taxpayer the tools to provide explanations, which the taxpayer cannot do if he or she genuinely does not know what those concerns are.

Question 4. Do you agree HMRC's assessment of impacts?

29. We note the proposed change is not expected to have any significant economic impact. This surprises us and if little impact is expected, we question its utility.
30. With regard to time taken, we have commented above on the 60 day period and that it will not be adequate in some cases. It is likely that average time limits for case completion may be reduced as CDF will allow one-off disclosures without the need for a minimum amount of tax, perhaps even without a detailed report. However, cases that are currently dealt with under COP 9 are still likely to take a long time.
31. We have a concern that the need to admit fraud and the requirement to identify the amount involved within a very tight timescale could discourage voluntary disclosures by taxpayers who would have otherwise come forward, and therefore put revenues at risk.
32. We are concerned about the reference in a public document to 'small firms of accountants who represent fraudulent taxpayers'. We assume that this is intended as a reference to consultancy firms that deal with CIF cases of taxpayers for whom they do not deal in a day to day capacity. However that is not clear from the wording adopted.
33. We have a concern that tight time limits may drive smaller firms of accountants that currently handle CIF cases as part of normal day-to-day business away from dealing with such cases. A firm that has to balance dealing with a CIF case against, say, dealing with the sale of a client's business is far less able to comply with tight time limits than a larger firm with a specialist investigation department. While we can see a case for discouraging 'amateurs' from dealing with CIF cases, there are general practice accountants with the expertise to handle such work. We think that it would be a retrograde step to create a system that discourages taxpayers from using such accountants for an investigation. Our comments on the 60 day time limit and on the format and content of the OD are relevant here.

OTHER COMMENTS ON THE PROPOSALS

Case selection

34. In order for the CDF to work, it is crucial that HMRC selects the right cases, where good research and good risk assessment provide reliable evidence that there has been fraudulent activity.
35. The accusation of fraud is a serious one and should not, due to poor research and case selection, be levelled at those who are not guilty. This is particularly important with the CDF because taxpayers may feel obliged to admit to fraudulent activity, because of the fear of prosecution, even if any irregularities in their affairs do not fall into the category of fraud.

The outline disclosure document

36. Paragraph 4.8 sets out what the OD might contain, which suggests that the OD is expected to be fairly detailed.
37. We do not think that HMRC should be too prescriptive about precise details at the OD stage. For example, it may be possible to provide an estimate of the amounts involved at an early stage, but the actual figures may turn out to be rather different as the detailed report is prepared. If the estimated and final figures were markedly different, would the taxpayer risk losing the benefit of the CDF, assuming that the estimates were provided in good faith? And it may also be difficult to identify all the entities affected and parties involved at the OD stage, as this information may only emerge in full as the detailed report is prepared. Again, we trust that the taxpayer would not be at risk of losing the protection of the CDF if the OD did not detail every entity or party involved.
38. If HMRC makes the OD too prescriptive it may deter taxpayers from accepting the CDF.
39. We are also worried about the need for the outline disclosure to include an admission of fraud in relation to each irregularity disclosed. It is reasonable for it to include a general admission of fraud. However, fraud requires both a knowledge of the law and an intention to break it. A person who diverts business takings into an overseas bank account, for example, has knowledge that diverting the funds is fraud; he or she may not have knowledge that not declaring the overseas bank interest is also fraud. The taxpayers ought to be entitled to acknowledge that he or she has committed fraud without having to take advice as to which transactions were fraudulent and which were not. This is an area that many advisers are not competent to advise on, let alone expect the taxpayer to recognise.
40. We are also unclear how HMRC would define a single fraud. For example, in the situation outlined above, would the diversion of funds and failure to declare interest on them be regarded as one fraud (since it all relates to the same initial diverted funds) or separate frauds? This will need to be made very clear in the guidelines for completing an OD.

The certified disclosure document

41. We understand that HMRC will not prescribe the format of the certified disclosure (CD). The format will depend on the case. Some cases may require a full report in the traditional way, but this would not be needed in some simpler cases.
42. We agree that there should be flexibility about the nature of the CD, but HMRC must provide some guidelines setting out the minimum requirements and what the CD might look like in a range of cases. This will be essential given that the CD will be a prosecutable document, particularly where the taxpayer does not have an adviser or the adviser is not a specialist in this field. The case officer should also be prepared to discuss and agree the format and contents of the CD.

Code of Practice 9

43. Code of Practice 9 will need to be re-written to reflect the CDF. When this is done, we recommend that style and structure are changed in order to make quite clear who it is aimed at, what it involves, the advantages of accepting the CDF route and the disadvantages of non-cooperation. There is a view that the current COP9 does not sufficiently stress the seriousness of the situation and even gives the impression that there will be no prosecution even if there is a total lack of cooperation/disclosure.
44. HMRC should also bear in mind that by doing away with the monetary limits for identifying 'serious' cases suitable for COP9, the CDF will bring in more lower-income or unrepresented taxpayers – and inexperienced advisers – who are not familiar with the concept of fraud or

with HMRC's civil and criminal investigation procedures. HMRC must clearly explain the terms and procedures used in its guidance.

The role of the adviser

45. We are pleased to note that HMRC intends to recommend that the taxpayer gets suitable professional advice.
46. We understand that HMRC is considering whether to contact the authorised agent, if there is one, when the CDF offer is sent to the taxpayer. We support this suggestion, although HMRC should bear in mind that the regular agent may not have specialist knowledge of fraud or HMRC's investigations procedures. It will therefore be important for the agent letter to make clear what is being proposed.
47. We understand that advisers will be able to request CDF for suitable cases. They would need to give HMRC the taxpayer's name and address, but not details of the wrongdoing, so HMRC can check if the case is already being worked – if not, HMRC would be able to offer CDF. We welcome this.

Unrepresented and low-income taxpayers

48. We note that the CDF will no longer use the term 'serious fraud' (on the grounds that this is hard to define) and will just refer to 'fraud'. HMRC is also doing away with the monetary limits used to identify cases suitable for CIF, to be handled either by the CIF teams or Special Investigations. Thus cases involving small amounts will come within CDF.
49. As noted above, this will bring in cases which would not now be dealt with under CIF, involving taxpayer on relatively low incomes who may be unrepresented, and taxpayers with agents who are not specialists. HMRC's own staff handling CDF may not be used to dealing with such cases.
50. Under its charter obligations HMRC should provide all necessary support and information to such taxpayers selected for the CDF. HMRC should bear in mind that some taxpayers may not be able to afford specialist advice.

JMM

E jane.moore@icaew.com

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APPENDIX 1

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.