

New Guidelines for Compliance: HMRC bolsters its evolving compliance assurance strategy

The rollout of a new tax administration programs rarely garners as much attention as tax policy announcements. First announced in November 2021¹, a new HM Revenue and Customs (HMRC) program, "*Guidelines for Compliance*"² (GfC), may therefore have gone unnoticed by many large business taxpayers, particularly those headquartered outside the UK.

It would be a mistake to remain uninformed, however. While on the surface the GfC program may seem innocuous and unremarkable – even helpful to taxpayers – in practice it may have significant implications and is part of a wider long-term compliance assurance strategy pursued by the UK in tandem with other tax authorities which may in due course lead to a changed relationship between taxpayer and revenue authority.

Guidelines for Compliance take the form of a series of HMRC documents designed to make clear HMRC's view on what HMRC believes to be "complex, widely misunderstood, or novel areas of the tax rules"³, and the first title in the series, on Pay-As-You-Earn (PAYE) settlements, was released in early October 2022⁴.

¹ As part of a wider review of tax administration for large businesses – see

<https://www.gov.uk/government/publications/review-of-tax-administration-for-large-businesses>

² See <https://www.gov.uk/government/publications/how-guidelines-for-compliance-gfc-help-you-with-tax/about-guidelines-for-compliance>

³ Ibid.

⁴ See <https://www.gov.uk/government/publications/gfc1-2022-guidelines-for-compliance-help-with-payee-settlement-agreement-calculations>

GfCs may apply to any tax or duty administered by HMRC, or to an issue that involves more than one tax or duty. A GfC title will accompany each major new piece of legislation, while changes to existing legislation should also be accompanied by an updated GfC document, where one already existed. Taxpayers who have interacted with the Australian Taxation Office's (ATO's) Practical Compliance Guidelines (PCGs) will immediately be aware of the similarities.

Describing the reasoning behind the program, HMRC notes that the business community has for some time requested greater transparency and clarity to help them manage their tax risks. Put another way, businesses continue to seek tax certainty, and better transparency as to the tax authority's interpretation of complex issues is presumably seen by many tax authorities as a helpful step in that direction.

The goal of GfC, says HMRC guidance, is to extend existing publications beyond the interpretation of the law, helping taxpayers to better understand HMRC's expectations and compliance processes. In each GfC publication, HMRC will share its view of the most common risks, highlighting approaches that it believes may lead to errors and possibly HMRC tax assessments. HMRC further promises to share practical approaches within the GfC publications that will help taxpayers lower their risk of non-compliance.

The GfC publications (which we can expect to build into a more comprehensive library over time), says HMRC guidance, will highlight those interpretations (by taxpayers) that have a higher risk of non-compliance with UK tax law, and instead suggest alternative, compliant paths. They may also set out HMRC's preferred treatments and methods when calculating the tax due for some transactions. Finally, GfC may also highlight what HMRC perceives or expects to be common problems to avoid, as well as sharing leading practices to consider when following a particular compliance process.

A layered approach

The GfC series will not replace HMRC's existing guidance, which is typically housed in technical manuals and other HMRC publications. Instead, it will aim to help taxpayers understand and comply with the legislation, while also giving them more insight and detail in areas where HMRC thinks the tax paying community may benefit from additional guidance. Importantly, GfC do not represent any form of safe harbor, and following a GfC to its exact letter in no way means that a return or other filing or disclosure will avoid being checked, says HMRC⁵. In that regard, they represent HMRC's interpretation, with which taxpayers may or may not agree.

⁵ See <https://www.gov.uk/government/publications/how-guidelines-for-compliance-gfc-help-you-with-tax/about-guidelines-for-compliance>

GfC could also potentially be a key place where taxpayers will be able to ascertain HMRC's known position for the purposes of the new requirement (as of 1 April 2022) for businesses to notify HMRC of any Uncertain Tax Treatment (UTT)⁶.

More on the first – and next – GfC documents

As noted, the first GfC to be published is on PAYE Settlement Agreements⁷; The GfC document outlines HMRC's preferred method of submitting calculations for PAYE Settlement Agreements (PSAs) and is intended to help employers reduce the risk of error when calculating amounts of income tax and Class 1B National Insurance contributions payable for benefits in kind and expenses accounted for with a PAYE Settlement Agreement. It highlights a number of errors and risks that HMRC sees in reviewing PSAs and sets out what HMRC expects to see in relation to these. As examples, the new GfC covers:

- HMRC's preferred method for submitting calculations (form PSA1, submitted digitally)
- Ways to help employers to reduce the risk of inaccuracies and errors when calculating income tax and class 1B NICs on benefits in kind and expenses accounted for under PSAs

⁶ The UTT requirements apply to treatments which may have tax consequences of more than £5 million. You can read more about the UTT requirements in this EY Global Tax Alert: https://www.ey.com/en_gl/tax-alerts/uk-notification-by-large-businesses-of-uncertain-tax-treatments

⁷ See <https://www.gov.uk/government/publications/gfc1-2022-guidelines-for-compliance-help-with-payee-settlement-agreement-calculations>

- Detailed suggestions and reminders for calculations (for example, accounting for different tax rates in Scotland and Wales, using representative samples, dealing with employees who pay no tax, grossing up tax and dealing with employees who pay social security contributions in other countries)
- Examples of how to calculate NIC contributions values
- Guidance on NICs timings (including the interaction of class 1, 1A and 1B NICs)
- Expectations around taxpayer's record retention.

While a prospective list of future GfCs is not yet available from HMRC, it is interesting to speculate what further areas HMRC might consider suitable for future GfCs. HMRC may want to target areas where it believes it is seeing widespread uncertainty based on current compliance activity, or instead may focus on new taxes or changes in tax policy, with a view to supporting those. HMRC recently released an interactive 'decision tool' to help businesses determine if they qualify for the new super-deduction or special rate first year allowance on plant or machinery costs⁸, so this is an area where we might reasonably expect to see a GfC in the near future. The Australian experience may also be informative in this regard (see next section).

Analysis of HMRC's objectives

Nothing like the GfC program has ever been previously attempted in the UK. With tax authority representatives meeting regularly under the auspices of the Organisation for Economic Cooperation and Development's (OECD's) Forum on Tax Administration

⁸ <https://www.gov.uk/guidance/check-if-you-can-claim-super-deduction-or-special-rate-first-year-allowances>

(as well as within their own regional groupings), it should be no surprise to taxpayers that ideas implemented by one jurisdiction are quickly replicated by others. Consider, for example, the way in which both Australia and the UK designed new programs to tackle perceived tax avoidance by large companies within 12 months of each other - the UK with the 2015 Diverted Profits Tax (DPT), and Australia with 2016's Multinational Anti-Avoidance Law (MAAL). So-called 'nudge letters' - targeted communications from a revenue authority to those taxpayers whose tax affairs they suspect may not be fully in order - are a similar innovation, with the ATO in this case being the original creator.

In the case of HMRC's *Guidelines for Compliance*, the inspiration is likely found in the ATO's PCG program. First introduced in 2016, the ATO either published or updated 63 PCGs between 2018 and 2022, spanning a broad spectrum of topics across multiple tax types⁹. Example topics include 'Diverted Profits Tax' (PCG 2018/5), 'Transfer pricing issues related to inbound distribution arrangements' (PCG 2019/1), and 'Non-commercial business losses - Commissioner's discretion regarding flood, bushfire or COVID-19' (PCG 2022/1).

The experiences of taxpayers in Australia with the ATO's PCGs may well provide an indication of how the UK project might over time be perceived by those impacted. While it is fair to say that PCGs are actively taken into consideration by affected taxpayers in Australia, that is not to say that their existence is received exclusively

⁹ You can view available PCGs in the ATO legal database: <https://www.ato.gov.au/law/#Law/table-of-contents?docref=PCG>

warmly. "Several PCGs require taxpayers to either rate or categorize transactions or tax attributes," says Fiona Moore, EY's Sydney-based Oceania Tax Controversy Leader. "As such transactions and attributes are also disclosed in the context of Category C of Australia's Reportable Tax Positions (RTP) schedule¹⁰, PCGs are used directly by the ATO not just as helpful guidance, but as an active risk assessment tool."

Furthermore, PCGs represent the ATO's risk assessment methodology and do not actually represent actual tax law - but are often treated as such. "It can be very easy to have an escalated risk rating under a PCG, so in this regard many taxpayers actually query their utility," says Fiona. "If we take for example PCG 2017/4 (Describing the ATO's compliance approach to taxation issues associated with cross-border related party financing arrangements and related transactions) - it's a reasonably narrow set of circumstances that will get you into the green zone, while an interest free outbound loan gets you into the orange zone (the second highest zone), before any other factors are even considered."

It may be fair to assume that taxpayers impacted by HMRC's GfCs might also develop similar perceptions over time. That should be of little surprise, as HMRC's strategy in deploying the program is quite clear: while HMRC may want to provide taxpayers with

¹⁰ The RTP Schedule was introduced by the ATO in 2011. It is designed to assist the ATO in gathering information on the uncertain tax positions of the largest public and multinational companies. The scope and content of the RTP Schedule has expanded over time, and now covers large public, foreign-owned companies as well as privately owned businesses. Although different in many regards, a broad comparison can be made between RTPs and the United States' Uncertain Tax Positions as set out in FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" (FIN 48). As a side note, the UK's HMRC has also introduced a similar concept to FIN 48 in 2022, the Notification of Uncertain Tax Treatment (NUTT) for large businesses.

clarity on how an issue will be treated, taxpayers deviating from “acceptable” treatments or interpretations as outlined in a GfC document may well find themselves on the receiving end of an enquiry or audit. To continue the Australian analogy, taxpayers may feel the need to “swim between the flags” in order to avoid receiving examination from the tax authorities. It remains to be seen what the implications of venturing outside the flags may be and, indeed, whether the space between the flags narrows over time.

Final thoughts

Large business taxpayers should be under no false impression that the relationship between taxpayer and revenue authority is shifting and evolving over time. The notion of co-operative compliance programs – whereby taxpayers agree to greater transparency and sharing of tax positions with a revenue authority, often in real time, in return for the promise of reduced compliance interventions – has been a quiet yet steady part of many revenue authorities’ compliance strategies for some time.

Cooperative compliance can be a highly resource intensive activity, however, and more recently, and in line with the position adopted by the OECD, we have seen an evolution in the approach as tax administrations try to move away from costly ‘downstream’ interventions (i.e., audit activity) and increasingly focus on “compliance assurance”. Under the compliance assurance ethos, the onus is put firmly on the taxpayer to prove that not only are their numbers right, but that the governance, processes and controls via which they reached those numbers (often referred to as

Tax Control Frameworks) are also robust and sustainable. A growing number of revenue authorities are deploying new compliance assurance programs (some voluntary and some mandatory) where the presence (or not) of effective tax governance is used to categorize taxpayers into different risk segments.

HMRC was one of the earliest adopters of these models and re-affirmed its commitment to compliance assurance with the re-launch of its Business Risk Review+ (BRR+) program in 2019. GfC takes the compliance assurance ethos one step further; while indeed providing businesses with guidance, the program effectively provides HMRC with a further set of tax guiderails within which businesses must operate – or face the consequences.

While the first GfC on PAYE Settlement Agreements represents a relatively straight forward topic, as HMRC becomes more confident in its application of this new tool we can expect HRMC to follow the ATO's lead in taking on more interesting (and controversial) areas, including transfer pricing. Businesses would be well advised to keep a close eye on developments in this space, both in the UK and elsewhere.

Policy replication – the tax world's way of saying "imitation is the sincerest form of flattery" – should be expected in this area, with other revenue authorities deploying similar programs, though it is notoriously difficult to define a timeline under which such replication might occur. As quickly as countries (including, most recently, Malaysia and Singapore) are deploying new compliance assurance programs, so too then we should probably expect other countries to pick up on the GfC approach and replicate it. Taxpayers should therefore ensure they are fully aware of – and prepared

for – the evolving compliance assurance ethos, and that their own approach to tax governance and control is sound – including not only testing their own positions against HMRC’s GfC, but also looking more widely to see which revenue authority might be next to adopt this approach.

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