Taxing Matters

Navigating the complexities of the tax world

RPC

Season three, episode two – Crystal ball gazing with Jasprit Singh

Alexis: Hello and welcome to Taxing Matters, your one-stop audio shop for all things tax brought to you by RPC. My name is Alexis Armitage and I'm a Senior Associate in RPC's Tax Disputes team. I will be your guide as we explore the sometimes hostile and ever-changing landscape that is the world of tax law and tax disputes. Taxing Matters brings you a roadmap to guide you and your business through this labyrinth. In case any of you miss any crucial information or just want some extra bedtime reading, there is a full transcript of this and indeed every episode of Taxing Matters on our website at www.rpclegal.com/taxingmatters.

I'm delighted to be joined today by one of my colleagues in the tax team at RPC, Jasprit Singh. Jas is a Senior Associate and specialist in tax disputes and investigations and acts for a wide range of clients across all sectors. Jas' focus is primarily on tax disputes and investigations. He has extensive experience representing clients, both corporates and high net worth individuals in HMRC inquiries and investigations all the way through to litigation and has appeared before the First Tier Tax Tribunal, Upper Tribunal, Court of Appeal and Supreme Court. Welcome, Jas, and thank you for joining me today.

Jas: Hello Alexis and thank you for having me today.

Alexis: Today, Jas and I are going to be doing a bit of horizon scanning by discussing the areas and targets that HMRC, under a Labour government, are likely to focus on next. At high level, Jas will talk us through some of the big themes that might be coming up that are of interest to taxpayers and tax advisers focusing on three overarching topics. So, we'll start with Labour and the autumn budget, the likely target areas for HMRC, and also the role of AI in HMRC's plans. So without further ado, Jas, shall we start with Labour and the Autumn Budget?

Jas: With the date of the autumn budget drawing closer, we can start there. Interested parties will be following any information shared by Rachel Reeves very closely during this period. As the Chancellor of the Exchequer prepares to present the first budget of Labour's new parliament on 30 October 2024. One of the key issues raised by Labour is that they have inherited a £22bn black hole from the previous Conservative government. The key question becomes, how will Labour deal with this? As they have already ruled out increases to income tax and national insurance to plug this gap, there has been much speculation as to how the gap will be closed. One area of speculation relates to the planned changes to the taxation of non-UK domiciled individuals, originally announced by the Conservative government at this year's spring budget. The regime is relevant to the taxation of people resident in the UK, but whose domicile is considered to be outside the UK. Under the current regime, these individuals can elect to pay tax on the remittance basis, which means they pay tax on UK income and gains in the same way as UK domiciles but only pay tax on foreign income or gains when it is remitted, in other words, brought into the UK. In a recent policy paper, the Labour government confirmed its commitment to Labour's pre-election pledge. The government stated that it is committed to addressing what it regards as unfairness in the tax system, so that everyone who is long-term resident in the UK pays tax here. The government therefore intends to remove the outdated concept of domicile status from the tax system, and implement a new residence-based regime, which it considers to be internationally competitive and focused on attracting the best talent and investment to the UK. Rachel Reeves has also previously said that she wants to outright end non-domicile status, but there have been recent indicators which suggest a softening of this approach, with the Chancellor mentioning that she was ready to water down those proposals if it would fail to raise the £1bn it hopes to gain.

Further, the implementation of the planned changes may not have the desired impact. For example, a recent report from Oxford Economics warned of Labour's proposed non-domicile changes, citing that 98% of remittance basis users surveyed, indicated that they would emigrate from the UK sooner if the reforms were implemented and the resulting tax loss of £1bn to the Exchequer. How much weight can be placed on this is uncertain as the research methods are unclear and the report acknowledges that a behavioural response is highly uncertain. However, there is definite concern in relation to people leaving the UK. Therefore, other areas could be the focus for Labour. For example, there could be changes to capital gains tax. Although the Chancellor stated she has no plans to align CGT with income tax rates, she has not ruled this out. With the highest CGT rate currently at 28%, well below the top 45% rate of income tax, some, such as the HomeOwners Alliance, think that this might be increased in line with income tax to raise additional revenue. The Institute for Fiscal Studies has estimated that aligning CGT with income tax could raise over £16bn for the Chancellor. However, there are significant concerns that such an increase would have unintended consequences, particularly for those looking to sell their businesses. Entrepreneurs who were considering selling in the near future may now be accelerating their plans to avoid a higher tax bill if rates increase. This could also prompt business owners to retire earlier than anticipated or even leave the UK altogether for jurisdictions with more favourable tax regimes. Additionally, while an increase in CGT may seem imminent, there is also a risk that such a move could lead to a decrease in the overall tax take, as investors may choose to hold onto their assets longer rather than incur higher tax rates.

Business property relief may also be subject to change under the new budget. It was originally introduced as a relief to inheritance tax to ensure that family-owned businesses or farms could continue to trade after a death. However, there are rumours that Labour might bring a cap to business property relief to £500k and also bolster more stringent requirements before eligibility kicks in. This might mean the level of trading activity required, currently at 50%, is increased to 80%. The potential changes have caused a considerable stir and it will be interesting to see what Labour will do.

Alexis: Great, thank you, Jas. So now you've set the scene. Shall we take a closer look at some of the areas and targets that HMRC under a Labour government are likely to focus on next?

Jas: In broad terms, it is possible that HMRC's activities may increase under Labour if the funds promised by Labour are invested into HMRC investigations and the hiring of more tax inspectors. Large corporates and high net worth individuals are generally focus areas for HMRC as they can offer HMRC the possibility of collecting large sums of tax. Investigations into such groups can also be more prolific in acting as a deterrent to other taxpayers. HMRC may renew and increase their focus into these areas, however, as for example, large corporates have come under public scrutiny again. This is based on recent reports that large online retail businesses may be paying less UK tax in contrast to the scale of their UK business activities. HMRC have already benefited from collecting additional tax from previous years through focused efforts and investigations into multinational businesses allocating profits to overseas ventures. These efforts may continue and HMRC may start more investigations into large businesses.

High net worth individuals are also likely continue to be one of HMRC's focus areas, not least because of the success HMRC have had with the tax collected in the case of Bernie Ecclestone, but also as part of its wider criminal investigations resulting in, it is reported, the collection of £991m in 2023-2024. With the direction set by Labour to crack down on tax avoidance, it is likely that investigations by HMRC may increase.

In addition, HMRC can rely on recent legislation and new powers, building on existing ones to further target promoters of tax avoidance schemes and tackle tax fraud. Specifically, the measures contained within sections 32 to 34 of The Finance Act 2024 create a new strict criminal liability offence for failing to comply with the stop notice issued by HMRC. HMRC can also now apply for directors to be disqualified where that person is connected with the promotion of a tax avoidance scheme. Prior to the enactment of this provision, HMRC could not apply to the court itself for a director's disqualification order and had to refer the case to the Insolvency Service if it wished to have a person disqualified from being a director. If other trends are any indication, it is likely that HMRC will grow in confidence to rely on new offences, and their powers, to tackle tax avoidance. For example, the screws are being tightened in other ways too, as HMRC attempts to crack down on suspected criminal behaviour. HMRC has dramatically increased its use of account freezing orders and forfeiture orders in the last three years, according to the results of a Freedom of Information request, with the value of assets being seized in 2023/24, totalling £57m. According to this data, the number of account freezing orders has increased from 125 in 2021/22 financial year, to 341 in 2023/24, representing an increase of more than 170% over the three-year period. The evidential threshold for obtaining an account freezing order is low and concerning for businesses, due to the potential impact on operations it can have, even where there is no subsequent successful forfeiture of assets or criminal prosecution. Another area of focus which is likely to continue for HMRC is in relation to research and development (R&D) tax relief. Notably, recent raids by HMRC have resulted in eleven arrests across the UK in relation to suspected fraud involving R&D tax relief programmes. This includes two companies in Norwich called Green Jellyfish and Kirby and Haslam, which were subject to an investigation. HMRC are likely to continue to crack down in this area due to the potential for fraud.

The increasing regulations and HMRC crack down appears to already have impacted the number of claims, as commentators have noted that there has been a 21% drop in R&D tax credit claims for the 2022/23 tax year as companies are being more cautious in claiming the relief. On the whole, HMRC show little sign of slowing in their attempts to tackle tax avoidance and tax fraud.

Alexis: So Jas, what about the role of AI in HMRC's plans? How does that fit in?

Jas: AI is certainly something HMRC are using already in some ways, such as through its current "Connect" system, to analyse data it collects. We can also see that HMRC are giving further consideration to the potential ways AI can assist with and improve the administration and collection of tax. Notably, HMRC recently released an updated privacy notice about their use of AI. Some of the deliberated uses of AI for HMRC include using AI to nudge taxpayers to when they might need to file a tax return, for example following the issue of an updated tax code, and using AI to analyse large data sets to identify high-risk areas and individuals so HMRC has a more targeted approach to investigation.

Also, it was stated that HMRC would only use AI where the law allows them to do so for the purposes of the assessment or collection of tax. This should be treated with some caution, however, as the legal framework surrounding AI is still in its early days and there is no legislation yet on how HMRC might use AI. Therefore, many people will probably agree with the Institute for Fiscal Studies Tax Law Review Committee that practical steps should be taken to make HMRC's use of AI legitimate and acceptable, as well as to safeguard taxpayers. Indeed, it was recommended that there should be specific legislation and even a new HMRC AI charter. This recognises that one of the key concerns is that the current tax law relies heavily on the fact that decisions are taken by individual human HMRC officers and not by AI. As the AI space continues to move forward, including HMRC's potential use of AI, it will be important that HMRC is as transparent as possible about how AI is being used, what controls are in place, and how any decisions have been reached, which HMRC then acts upon in order to mitigate risks and safeguard taxpayers.

Alexis: Well thank you so much for your time and for doing some serious horizon scanning on the areas that HMRC are likely to focus on next, Jas. Unfortunately, that's all we've got time for in this month's episode. Thank you again to Jas for today's podcast.

As ever, a big thank you goes to RPC's in-house team for the production, music and sound editing of this episode. A full transcript of this episode together with our references can be found on our website at rpclegal.com/taxingmatters.

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