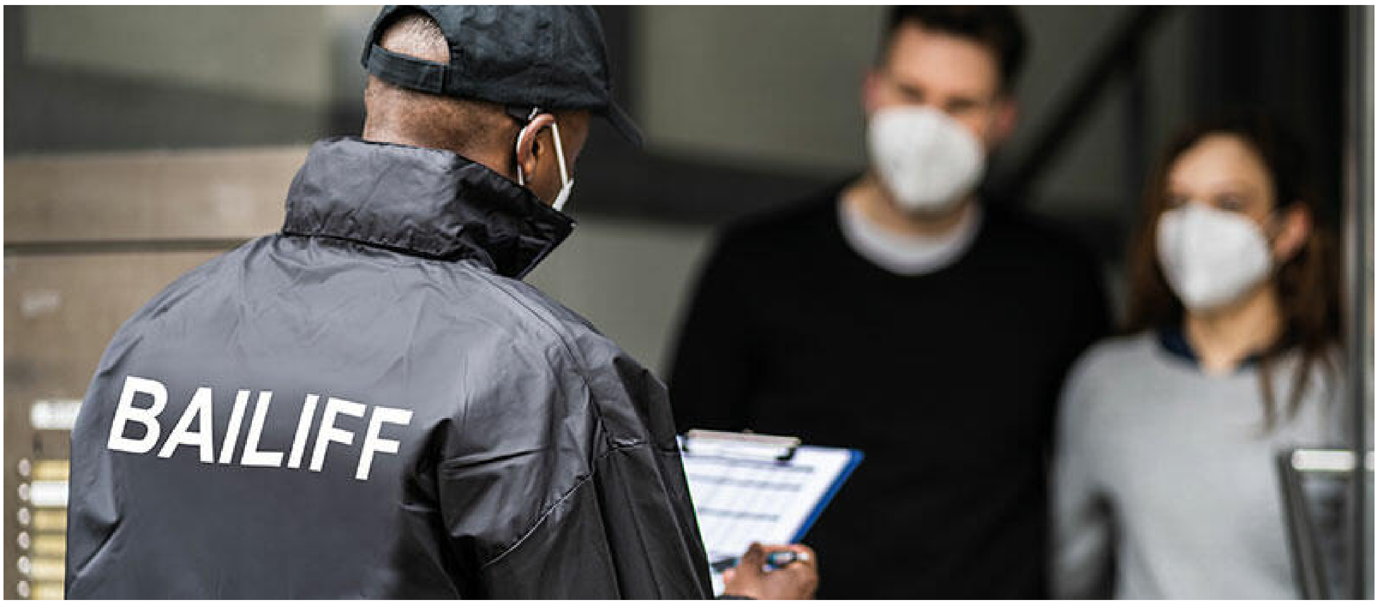
Avoiding enforcement action due to tax debt

Management of taxes OMB Personal tax



24 February 2022

With total tax debt of £39 billion, government measures to soften the pain during the pandemic are coming to an end. Here are some practical tips for taxpayers who need more time to pay.

Key Points

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What is the issue?

At 31 December 2021, total tax debt was £39 billion. Not only is this a result of more taxpayers being in debt, but an increase in the value of debt owed by individual taxpayers.

What does it mean for me?

As we emerge from the pandemic, and under the increasing threat of enforcement action and use of formal powers by HMRC, advisers should be encouraging taxpayers to actively engage with HMRC in respect of tax debts and agree TTPAs where required.

What can I take away?

With economists predicting that interest rates will continue to rise, tax debts are likely to be a growing problem.

Over the past two years, and in response to the extraordinary challenges faced by many taxpayers as a result of the Covid-19 pandemic, the UK government has provided extra resources to assist those struggling to pay their tax liabilities due to financial distress. However, as the UK comes out of the pandemic and the economy continues to reopen, HMRC will prioritise the collection of unpaid taxes.

This is unsurprising given the value of tax debt that accumulated over the pandemic. At 31 December 2021, total tax debt was £39 billion. Not only is this a result of more taxpayers being in debt, but an increase in the value of debt owed by individual taxpayers. Older debts alone, which are often more difficult to collect, increased in value from £2.5 billion in 2019/20 to £4.4 billion in 2020/21. (Note that tax debt is the difference between agreed tax liabilities and the amounts actually paid to HMRC. It does not include tax lost through tax fraud, avoidance or other errors.)

HMRC gave evidence to the Public Accounts Committee on 17 January 2022 about tax debt (see bit.ly/3Bv1M3o)

What additional support did HMRC provided during the pandemic?

In addition to the more ‘light touch’ approach involved in time to pay arrangements (TTPAs), which HMRC Debt Management have been able to agree with taxpayers for many years now, the following measures were introduced by the government during the pandemic in relation to tax debts:

Deferral of VAT

Businesses were able to defer VAT payments due between 20 March 2020 and 30 June 2020, initially to 31 March 2021. This deferral was extended to 31 March 2022, allowing taxpayers to spread the payment of their VAT liabilities over this period. This instalment period is shortly coming to an end and is unlikely to be extended.

Further time to pay leeway for hospitality and leisure businesses

On 21 December 2021, as part of the support for businesses affected by the omicron variant, the chancellor asked HMRC to offer businesses in the hospitality and leisure sectors in particular the option of a short delay and payment in instalments on a case by case basis (see bit.ly/3uZvMTO).

Deferral of income tax surcharge

On 6 January 2022, HMRC announced that the 5% surcharge for any 31 January 2022 Self Assessment liabilities paid late will not be levied, provided full payment is made (or a TTPA put in place) by 1 April 2022 (effectively a 28 day deferral). Interest remains chargeable from 1 February 2022 onwards.

Self-serve facility for TTPAs

Self Assessment taxpayers were permitted to set up a TTPA online, provided the debt is less than £30,000, they apply within 60 days of the payment deadline and they intend to settle the debt over a period of 12 months. In December 2021, HMRC confirmed that 123,000 individuals used the online service to spread the cost of their Self Assessment bills for the 2019/20 tax year, worth £460 million. More than 20,000 taxpayers used the service to spread £46 million of payments for the 2020/21 tax year at that date.

Suspension of enforcement action

HMRC suspended the use of its debt collection activities and enforcement powers, such as taking control of goods, court action and bankruptcy/insolvency, to collect tax debts until the end of September 2021.

So, what will HMRC do next?

HMRC's policy paper published on 30 June 2021, 'Collecting tax debts as we emerge from coronavirus (Covid-19)', outlined its intention with regards to collecting debts that had built up during the first 12 months of the pandemic. The message was simple: 'If you can pay your taxes than you should do so – but if you're struggling, we want to work with you and agree a plan based on your financial position.'

HMRC demonstrated its ongoing support for taxpayers through the continued agreement of TTPAs on more favourable terms, such as allowing payment over a longer period of time (not writing off of taxes due) than what would have been agreed pre-pandemic. However, the policy paper also noted that from September 2021, HMRC would recommence debt enforcement action against taxpayers who are unwilling to discuss their debts or simply ignored HMRC's attempts to contact them.

Such action or use of debt collection powers may include:

- taking control of goods;
- tax collection through coding notices;
- direct recovery of debts from a taxpayers' bank and building society accounts;
- joint and several liability notices making directors and LLP members jointly and severally liable for tax debts in situations involving tax avoidance, evasion or pheonixism;
- notice of requirement to give security for tax debts; and
- bankruptcy/insolvency in the most serious situations.

See my article 'Tax debt collection' (*Tax Adviser*, August 2020), which examines HMRC's collection process and some of its powers in more detail.

Whilst we are yet to see HMRC return to the use of its full powers to collect tax debts, we have seen a shift in its approach to recovering the vast amount of taxes owed.

It does appear from our experience that as a precursor to enforcement proceedings, Field Force agents are starting to visit premises of business that have tax debts owing as a result of the pandemic.

HMRC gave evidence on tax debt to the House of Commons Public Accounts Committee in January, when officials confirmed that 110,000 field visits were carried out in the previous 12 months. HMRC announced that in the first instance, these visits focused on making sure that taxpayers were aware of their debt and the support available to them, as well as asking about their financial situation and ability to pay. This is seemingly in line with the policy announced by HMRC in June 2021.

Ultimately, it is only a matter of time before HMRC uses its formal powers with an eventual move towards increased use of bankruptcy or insolvency proceedings as a final sanction to truly distinguish those who cannot pay versus who choose not to do so.

As well as a gradual return to use of its existing debt collection powers, HMRC is focused on improving the collection of tax debt in the long term. Two recently published discussion documents, ‘Preventing and collecting international tax debt’ and ‘Call for Evidence – Modernising tax debt collection from non-paying businesses’demonstrate HMRC’s intention toevolve its approach to tax debt collection, and perhaps even powers, to keep pace with the evolving nature of the economy and business practices.

Therefore, as we emerge from the pandemic, and under the increasing threat of enforcement action and use of formal powers by HMRC, advisers should be encouraging taxpayers to actively engage with HMRC in respect of tax debts and agree TTPAs where required.

Time to Pay Arrangements: practical tips

Owing to the various tax deferrals offered by HMRC during the pandemic and the pause on collection proceedings during that time, some taxpayers will have built up potentially significant tax debts that they are unable to settle immediately.

Unlike assessments of tax, HMRC is not bound by time limits in relation to the collection of tax debt and it must therefore be proactively managed.

For those taxpayers who believe they will be able to pay what is owed over a period of time, they can seek HMRC’s agreement to a TTPA. Obtaining a TTPA gives the taxpayer certainty over this aspect of their cashflow and also puts a hold on further enforcement action by HMRC, provided the terms of the TTPA are adhered to. The imposition of late payment penalties can also be avoided where a TTPA application is submitted before the trigger date for such penalties and a TTPA is subsequently agreed.

Taxpayers should therefore be actively considering how they can afford to settle any debts owing to HMRC which have been deferred during the pandemic. Actively approaching HMRC to discuss the payment of tax debts over an agreed payment plan can often lead to more beneficial TTPAs being granted compared to taxpayers who simply try to avoid the situation in the hope that it goes away.

Where using the self-serve facility for Self Assessment taxpayers referred to above is not possible, it is necessary to contact HMRC directly to discuss the tax debts owing with a view to agreeing a TTPA. With HMRC reverting back to its pre-pandemic criteria when considering a TTPA request, taxpayers should be prepared to discuss:

1. the financial hardship and impact of Covid-19 on their finances;
2. the actions taken to pay the tax due. This may include, for example, details of other funding options explored and how other costs have been reduced. HMRC wants reassurance that borrowing and overdraft facilities are maximised. For corporate debts in particular, HMRC expects the owners and other stakeholders to contribute financially to support the business. If necessary, the shareholders may also be expected to inject some of their personal wealth into the company;
3. what assets can be realised to settle the tax due;
4. any tax refunds due to the taxpayer (for example, VAT reclaims or research and development claim repayments) that can be offset against the tax debts due;
5. their repayment proposal to settle what is owed to HMRC, including their rationale for the quantum of regular instalments and period covered by any TTPA. HMRC may expect a significant upfront payment and will not ordinarily agree to ‘payment holidays’;
6. why they consider their proposed repayment schedule is affordable; and
7. other financial information that can be submitted to HMRC in support of the proposal, if requested. For individuals, this may include an average monthly income/expenditure summary and for corporates, a cash flow forecast.

HMRC will also seek reassurance that the taxpayer intends and is able to settle all future tax liabilities as and when they arise. It is crucial that taxpayers put forward their ‘best offer’ to HMRC to avoid a straight rejection and escalation of the tax debt along the enforcement process. Whilst HMRC will not always agree a TTPA, perhaps due to the requested TTPA period being too lengthy or the ‘down payment’ being deemed insufficient, a proactive approach to dealing with tax debts is a must.

Should HMRC consider more radical solutions, such as partially writing off tax due or making it easier to deal with multiple tax debts, remains an open question. We remain concerned about the use of third party debt collection agencies and support for vulnerable or low-income taxpayers who may not have access to professional tax advice.

Advisers also need to remind taxpayers that forward interest is charged by HMRC on any underpaid tax and this accrues daily, with interest rates linked to the Bank of England interest rates. With economists predicting that interest rates will continue to rise, tax debts are likely to be a growing problem.