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# VAT disputes

Handling HMRC enquiries  
and disputes



# Introduction

In our previous **note**, VAT disputes in asset management - avoiding common disputes, we set out some of the most common VAT disputes we come across when advising asset managers and discussed ways of reducing the risk of such disputes arising.

In this note we discuss strategies for, and the practicalities of, handling VAT disputes. The matters discussed in this note are not specific to asset management but will be relevant to asset managers that find themselves in a VAT dispute with HMRC.

The following sections set out some common topics of disputes and steps that can be taken to mitigate the risk of dispute.



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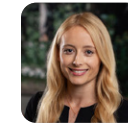
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# Form objectives, strategy and team

## Have a clear strategy and objective in mind



When dealing with any VAT dispute it is essential to have a clear strategy and objective in mind rather than only reacting to HMRC's questions and requests. A key part of achieving that is to identify who will be coordinating responses, who they will be assisted by, and to whom they will be reporting.

## Make early contact with HMRC



It is often helpful to make early contact with HMRC in person and to establish direct conversations as part of the enquiry process, whether to discuss practicalities or to raise more substantive issues. HMRC will request information or responses within a set time frame; such deadlines can often be extended but it is important to discuss extensions with HMRC rather than responding late.

## Document contact with HMRC



It is important to document contact with HMRC to ensure that there are no misunderstandings as to what has been agreed and what is happening next. Detailed notes should be kept for any material calls and meetings and can be agreed with HMRC.





# Gather information

## Supporting evidence

Typically, the burden is on the taxpayer to demonstrate that the tax position they are asserting is correct (rather than it being for HMRC to find fault). That colours HMRC's approach. It means that HMRC may have a checklist of questions they need to answer and it means that explanations will frequently need to be supported by evidence.

## Be in possession of all relevant information

It is better, therefore, to be in possession of all relevant information (whether supportive or not) from the outset.

## Document-destruction policy

If there is a document-destruction policy in place, it may need to be suspended. If there are individuals who have knowledge of the issues it will be important to ensure they are not going anywhere without first providing their insight.





# Predict and quantify potential results from the outset, identifying all potential arguments and vulnerabilities

## Have a clear understanding of the desired results

Arguments put to HMRC will usually be more focussed, and therefore effective, when the person making them has a clear understanding of the result they are seeking to achieve.

## Identify all potential issues early on

Identifying all potential issues early on will allow for the type of thorough information gathering exercise recommended above. Time and resources can then be spent on separating supporting evidence from matters which might distract from the business's key arguments, and should therefore be left aside. Importantly, the business will be in a better position to influence the direction of its discussions with HMRC, rather than simply reacting to arguments and requests for information.

## Consider all potential consequences of potential arguments and proposals

The business will also reduce the risk of arguments it puts forward having unforeseen consequences. For example, an asset manager might potentially be entitled to rely retrospectively on a use-based override to its partial exemption method to reflect a change in its activities giving a higher rate of VAT recovery. However, before making any such proposal the asset manager should consider whether there have been any other changes in its business which HMRC might argue have triggered a use-based override in HMRC's favour. Potential outcomes should then be quantified.







### **If the dispute is complex, identify which points represent “red lines”**



If the dispute is complex, the business will need to know which points it is willing to compromise on, and which represent “red lines”. Being able to take such decisions quickly will often give a tactical advantage and should at the least help to resolve the dispute more quickly. While businesses will invariably want to avoid litigation, the business will need to know whether litigation is a realistic possibility.

### **Inform others in the business of the potential outcomes**



Those responsible for handling the VAT dispute will be in a better position to inform others in the business (and the auditors, if necessary) of the potential outcomes.

### **Different deadlines may apply**



Different deadlines may apply depending on the arguments the business intends to pursue and having a clear plan from the outset will reduce the risk of deadlines being missed. We discuss the different deadlines which might apply in more detail below.





# Identify any relevant HMRC policies and distinguish between fact-based and policy-based areas of disagreement

## Distinguish between law and policy



It is important to distinguish between law (legislation and case law) and HMRC policy (usually set out in HMRC's public notices, manuals and Business Briefs). The amount of tax due from a business is determined by law and HMRC's policy is only their interpretation of the law. In several instances the courts have found policies published by HMRC to be incorrect.

That being said, it will be far easier in practice for an individual HMRC officer to accept an argument that aligns with, or at least does not contradict, HMRC's published policy. If conceding a particular policy is likely to result in claims from other businesses then HMRC may well be prepared to litigate to defend the policy. Even if HMRC ultimately accept that an exception should be made to a policy in a given case, such a decision will usually only be made after deliberation by a policy team, which can prolong the dispute significantly.

It will therefore typically be easier to resolve a dispute as to whether the business's facts are such as to bring it within a particular HMRC policy than to resolve a dispute over whether HMRC's policy is correct.

It may be that the dispute is one of several involving different taxpayers, which all relate to a particular HMRC policy or practice. In such circumstances it can be very helpful to understand the nature and status of the other disputes and whether there is anything in the business's facts which might distinguish it from the other taxpayers. Liaising with industry bodies, peers and advisers can help to inform the business's approach.

Finally, if the VAT position adopted by the business relied on published guidance or a clearance from HMRC, the issue may not even (or may not only) relate to application of the law but to HMRC's practice. That is a matter that may only be challenged through judicial review, which has its own procedure and strict time limits.





# Actively manage the enquiry

## Calls and meetings



Enquiries can drift, particularly where the parties are only exchanging correspondence. Calls and meetings are an important component of any enquiry process and can help resolve issues more quickly (and with fewer misunderstandings) than written correspondence.

## Confirm who you are speaking with



It can be helpful to understand who at HMRC the taxpayer is speaking with and who is really making the decisions. Taxpayers typically speak with a case officer and they can have a fair amount of autonomy. However, it is often the case that they will be passing on responses from their technical team. Even in that case, however, the case officer may be the one dictating how the enquiry is progressed.

## Agreeing an action plan



In the case of complex enquiries with substantial exchanges of information, it can be helpful to agree with HMRC an action plan by which the taxpayer will provide information and HMRC will respond. Such action plans inevitably change as the enquiry progresses but can be helpful in keeping them on track.

## Agreeing an issues list



At the least, agreeing an issues list can be helpful in ensuring that both parties have a shared understanding as regards issues that have been resolved and those that remain open. It can also help to discourage the raising of new issues when a dispute has been ongoing for some time already.





# Know your rights

## Limits on what information taxpayers can be required to provide



Most enquiries are run on an informal basis, without HMRC needing to use their powers to require compliance. That is usually the best and most effective way to proceed but it is important for taxpayers to be aware of their rights. We note below some of the issues concerning time limits and deadlines but taxpayers also have rights when it comes to the management of any enquiry. Again, this will help to ensure that a proactive approach can be taken.

## Taxpayers



Taxpayers cannot be required to provide certain information, for example where it is not reasonably required; where it is legally privileged; or depending on the nature of the enquiry.

## Information from other parties



If information is to be sought from a third party or from overseas, there are conditions that HMRC must meet.





# Be mindful of time limits and deadlines

In a future note we will explore litigation formalities, including time limits and deadlines, in greater detail. However, a few of the main points to consider before a dispute proceeds to litigation are broadly as follows.

## Taxpayer corrections within a four-year time frame



For output tax an error in a previous return can ordinarily be corrected within four years of the end of the relevant VAT return period, whereas for input tax an error can be corrected within four years of the date on which the relevant return was due for submission. Effectively, therefore, taxpayer claims and HMRC assessments are ordinarily capped at a period of around four years.

## HMRC's deadline to raise an assessment



HMRC will be time-barred if they do not raise an assessment within a year of receiving all the information required to do so. If they do not raise their assessment within a year then they will usually only be able to assess for around two years' worth of VAT, rather than the usual four years' worth.

## Appealing or seeking a review



Once a decision and/or assessment has been made by HMRC the taxpayer will have 30 days to either seek a review by another HMRC officer or to appeal to the First Tier Tribunal. If the taxpayer opts for a review then HMRC will have 45 days to complete their review, which should result in them issuing a review decision. The taxpayer then has 30 days to apply to the First Tier Tribunal to appeal the initial decision and/or assessment and the review decision.







### Judicial review



HMRC increasingly rely on statements of practice and guidance to inform how rules are applied. Where HMRC act contrary to their practice and guidance, judicial review may be relevant. It is worth noting this route specifically, not just because it is increasingly prevalent but because the process for pursuing judicial review is complex and separate from the tax appeal process. In particular, if a taxpayer wishes to pursue judicial review then they must apply to the High Court promptly and, in any event, within three months of the relevant decision of HMRC. If, for example, a taxpayer alleges that HMRC have acted in breach of the taxpayer's legitimate expectation by resiling from a previous ruling then the taxpayer must identify the date on which HMRC resiled from the ruling and make its application to the High Court promptly and no later than three months from that date.

### Consider deadlines



HMRC will often request information or responses to specific questions within a set time frame. It is important to distinguish such requests, which are not ordinarily binding in law, from legally binding deadlines. If you do not think it will be possible to respond to HMRC in the time frame requested then it is, of course, advisable to let HMRC know as a matter of courtesy and so that they know the matter is progressing. In most cases, the business will want to conclude the dispute or enquiry as soon as possible in any event.





# Decide when to call for the enquiry to end

## Closure of an enquiry



There is naturally a reluctance to insist on the closure of an enquiry because that may just prompt litigation. However, sometimes an enquiry moves from addressing a defined, potential risk to fishing for any other issues.

## Delays



If there are delays or HMRC are unnecessarily prolonging an enquiry, there are ways of forcing HMRC to close the enquiry and to decide whether they genuinely consider there is a risk to be addressed. It is not uncommon for HMRC to decide in these circumstances that there is not enough to justify challenging a taxpayer's position.







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