

Comment

Why we should support HMRC's new approach to tax dispute resolution

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Last year Dave Hartnett, the Permanent Secretary for Tax at HMRC, took part in a *Tax Journal* roundtable discussion on dispute resolution (*Tax Journal*, 19 April 2010) and among other things said this: 'Behavioural changes are needed to make alternative dispute resolution work well. Taxpayers have to change, their advisers have to change, but tax administrations have to change most.'

In their subsequent article ('View from HMRC: dispute resolution', *Tax Journal*, 10 January 2011) Geoff Lloyd,

who heads up HMRC's Dispute Resolution Unit, and Anthony Inglese, General Counsel and Solicitor to HMRC demonstrated that HMRC are now embracing that change with a three-sided approach to dispute resolution which corresponds to and mirrors the principal drivers in mediation techniques.

Two of the drivers: maximising revenue flows, and reducing costs are to be expected; the third driver – improving customer experience – is not. Indeed, many might greet the news with a degree of cynicism. But I believe that cynicism is misplaced. One example of HMRC's approach to customer relationship improvement is the way some Customer Relationship Managers (CRMs) have written to their customers for feedback into their own performance appraisal asking the customer about their working relationship and what the customer thinks is working well and what is working possibly less well.

Apart from the very fact of elevating the value proposition of customer experience, the significance to be taken from it is that at the heart of most disputes lies a breakdown in a relationship and understanding the importance of the relationship lies at the centre of a collaborative dispute resolution process, which in some cases could include mediation.

I believe it is now time for taxpayers and their advisers also to consider (if not embrace) that change and their approach to the resolution of tax disputes. Litigation is usually seen as the only alternative to a negotiated settlement. But litigation is adversarial, time consuming, costly and unpredictable. It is often also not appropriate where a dispute arises due to a misunderstanding between tax payer and tax administration on facts, and possibly law. In the area of transfer pricing, and multifaceted cases having a heavy mix of fact in law, litigation should only be seen as the last resort with something else occurring in between. In *DSG Retail Ltd v HMRC* [2009] UK FTT 31 the transfer pricing methodologies and the comparables used could have benefited from a collaborative process and been resolved before getting to Court.

It was also notable that as a postscript to their decision (para 141), the Commissioners made an open invitation to anyone concerned with the case to write to them with suggestions about how the Tribunal might make changes to the procedures for such appeals. The Tribunal is now empowered to bring to the attention of the parties the availability of alternative dispute resolution procedures and to facilitate their use (The Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules, SI 2009/273, rule 3). But there is no requirement on either the Tribunal or the parties to do so. Yet.

Many think that a tax dispute is binary: fact and law. However, a tax dispute is often much more. A tax dispute is not just about the amount of tax that should or should not be payable. It covers

all situations in which HMRC and the customer or their agent have a difference in view. There are a range of causes which lie at the heart of any dispute and can cause a dispute to become intractable if one or both sides adopt entrenched positions in respect of it. In these circumstances it is necessary to understand the interests and needs underlying those positions since while by their nature opposing positions in dispute are irreconcilable, the interest and needs of the parties may not be.

I believe that cynicism is misplaced ... advisers should now consider taking up HMRC's offer of working collaboratively

Although it is perfectly possible for both sides in a dispute bilaterally to work out the causes of it, it requires a common approach and willingness on both sides to find a solution which can be an impossible challenge if entrenched positions have already been taken; especially if the principal cause of the dispute is a breakdown in the working relationship. It is in this situation that the techniques of mediation and the role of a mediator can best be put to use.

Mediation has been defined by the Centre for Effective Dispute Resolution (CEDR) as 'a flexible process conducted confidentially in which a neutral person actively assists parties in working towards a negotiated agreement of a dispute ... with the parties in ultimate control of the decision to settle and the terms of resolution'.

Mediation has been dismissed by some as a 'touchy/feely' technique. Not being part of the basic legal or professional training programme it can feel inherently alien. The hardest part of my training to qualify as a CEDR-accredited mediator was to ignore over 30 years of legal practice and realise that my role no longer required me to take ownership of the problem nor look to offer solutions. During the course of that training I questioned how there could be a place for mediation in a tax dispute. The mistake I was then making was to assume – as many do – that a tax dispute was a binary problem. In fact, this learning curve is one of the benefits that is already being identified from the mediation pilot study which HMRC are currently conducting.

HMRC accept that they do not have a monopoly of understanding how tax law should apply to a particular set of facts and circumstances and they want to work with customers to fully understand the relevant law, sharing and testing the strengths and weaknesses of their own arguments, as well as fully understanding and testing the strengths and weaknesses of the customers' arguments all before reaching considered view on the strength of their case.

That does not mean that HMRC are 'going soft'; any settlement would still need to have a robust basis in law – as it always has had to.

Customers and their advisers should also now re-examine their approach to any dispute and consider taking up HMRC's offer of working collaboratively to assist in the resolution of that dispute, especially where the parties have become entrenched. Let us all now embrace this change!