

Closing the tax gap: HMRC's approach to 'legal interpretation disputes'

Can HMRC minimise 'legal interpretation disputes' in such a complex tax system?

La-Day (21 July) saw the publication of a 'Transformation Roadmap' for the modernisation of HMRC and the UK's tax administration, focusing heavily on proposed measures to close the tax gap and stamp out non-compliance.

A brief but notable inclusion is the commitment to address 'legal interpretation disputes', that is, 'cases where there is no avoidance but where the customer's interpretation of the law, and how it applies to the facts of a particular case, result in a different tax outcome than that intended by the legislation', to which HMRC attribute £5.4bn of the £46.8bn tax gap.

HMRC propose to tackle this issue through 'clearer expectations in guidance products' and by 'pursuing available options for legislative changes in those areas most prone to a disputed legal interpretation challenge'.

HMRC's concern is not new, with the 'notification of uncertain tax treatment' rules having come into force three years ago with the aim of reducing 'the legal interpretation portion of the tax gap'.

However, the Roadmap raises the fundamental question of whether it is appropriate to label the proper application of the tax rules to a particular taxpayer's circumstances as a 'tax gap' at all. After all, any disagreement with HMRC over the application of the law to a particular case could fall within this category.

Does HMRC's calculation of this portion of the 'tax gap' assume that their own legal interpretation is correct? It is the role of the courts, not HMRC, to determine the correct interpretation of the law. As an illustration of the problem, see the recent example of *Osmond and others v HMRC* [2025] UKUT 183 (TCC), where the Upper Tribunal rejected HMRC's interpretation of the main purpose test in the Transactions in Securities rules.

Anti-avoidance provisions in particular have the potential for uncertain and broad application, given they are often widely drawn subjective tests that turn on the facts of each case, and require taxpayers to take a view on whether or not they are caught by the rules. HMRC have increasingly sought to apply these tests in a literalistic way (as was the case in *Osmond*), which risks extending their

reach beyond what was contemplated in the legislation.

This brings us to HMRC's proposed measures to tackle the problem. Although only articulated in vague terms as we await further developments, the suggestions raise more potential concerns.

First, the proposal for HMRC to publish clearer guidance is welcome but, as ever, reliance on such guidance must be approached with caution. While a useful tool for taxpayers to understand how HMRC interprets the law, HMRC guidance is not law, does not need to be followed by the courts or even by HMRC themselves, and taxpayers may rely on it only in very limited circumstances. It is not wrong for taxpayers to depart from HMRC's position as stated in its guidance where it is considered appropriate and in accordance with the underlying tax law to do so.

Second, it is of course open to HMRC to propose changes to the tax legislation where they consider that it is not achieving its intended effect, and Parliament can legislate against undesirable outcomes to disputes if they see fit, but the courts will still have the final word in interpreting that legislation. There is a lot more to explore here in terms of HMRC's proper role in the UK's tax legislation process, but the question again is whether this is an appropriate means for dealing with what HMRC perceive to be a 'tax gap'.

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It certainly feels legitimate for HMRC to seek to minimise the number of tax disputes, especially given the level of time and resource involved, but the Roadmap proposals have the potential to exacerbate the underlying causes, which to a large extent must include the sheer volume and complexity of tax laws. Again, this is not a new issue and while tax simplification would be welcome for taxpayers and HMRC alike, previous attempts have been abandoned, most recently with the closure of the Office for Tax Simplification. If further legislation and guidance by HMRC are to be introduced to deal with £4.5bn of 'legal interpretation disputes', an open question is whether this could in fact compound the existing issue by adding further volume and complexity to the tax code.

We wait with interest for further detail on how HMRC will seek to apply these measures in practice but, given that 'legal interpretation disputes' are a continued focus for the government, taxpayers and advisors should continue to ensure that they can properly justify (and support with evidence) the tax positions they are taking. ■

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CenTax recommends changes to protect family farms

CenTax outlines four potential reforms to better target the APR and BPR reliefs.

A key question for advisers is whether there will be changes to the draft legislation on the reforms to agricultural property relief (APR) and business property relief (BPR). As clients need advice now, it is important to consider how the Government may still change what has been proposed, mostly likely in the forthcoming Autumn Budget.

In this context, the Centre for the Analysis of Taxation (CenTax) recently published a report titled *The Impact of Changes to Inheritance Tax on Farm Estates*. The report uses HMRC data to consider possible changes. It is a substantial document that runs to 135 pages.

Should you take any notice of CenTax? CenTax is not a government body. It is funded by the Nuffield Foundation and the abrdn Financial Fairness Trust and is supported by the LSE and the University of Warwick.

In the last nine months, I have been invited to discuss the APR/BPR reforms with CenTax on three occasions and so I was interested to see what conclusions they had reached. Their work is very methodical with considerable financial analysis of the impact on farms and other agricultural holdings, but it remains an academic report about tax policymaking.

What does the report cover? The report is a major piece of work but it only looks at the farming sector and the conclusions and suggestions they make may not apply to other business sectors. My impression is that looking at all businesses was too big a task for the resources of CenTax.

The report endeavours to arrive at the Government's objectives behind the reforms and to suggest plausible alternatives to what has been proposed in the draft legislation. The quality of the empirical approach, the attempt