# On or off the record?

**Management of taxes**




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*George Gillham* and *Hartley Foster* provide an update on the plethora of information powers at HMRC's disposal

## Key Points

## What is the issue?

HMRC has extensive civil powers to obtain information and documents from taxpayers and third parties, including tax advisers. Since the new system of

information powers was introduced in FA 2008, the government has amended the legislation almost every year, including in relation to obtaining information from third parties; keeping up to date with the plethora of HMRC's information powers is yet another challenge that tax advisers face.

## What does it mean to me?

Areas of potential difficulty for clients include HMRC requests for a taxpayer's private records and unannounced visits to business premises by HMRC officers. HMRC requests for documents that cover both business and non-business matters, such as diaries, should be addressed with care, particularly where such documents contain sensitive personal or professional information. Tax advisers need to be aware that HMRC officers can demand certain information from them whether or not they are the client's tax agent. Tax advisers should seek expert professional help in appropriate cases.

## What can I take away?

Clients should be educated regarding record keeping. Tax advisers should ensure that, wherever possible, clients keep and maintain adequate records from the outset. Ideally, documents held by clients should be segregated, according to whether or not they constitute 'business records', and whether or not they may be protected from disclosure, particularly by reason of legal professional privilege.

Under FA 2008 Sch 36, an HMRC officer may, by notice in writing ('an information notice'), require the taxpayer, or a third party, to provide information or documents if the 'information or document is reasonably required for the purpose of checking the taxpayer's tax position'.

'Tax position' is defined in Sch 36, para 64 as a person's position as regards any tax, including:

a) past, present and future liabilities to pay tax;
b) penalties and other amounts payable in connection with any tax; and
c) claims, elections, applications and notices in relation to that person's liability to pay tax.

HMRC consider that an officer does not have to have evidence that a document will definitely affect the tax position, only that it is ‘reasonably required’ to carry out a check. However taxpayers (and tax advisers) should critically assess any assertion that a document is reasonably required. In *Long v Revenue and Customs Comrs* [2014] UKFTT 199 (TC), the First-tier Tribunal (‘FTT’) rejected HMRC’s contention that a doctor’s appointment diary was reasonably required.

A person served with an information notice must provide the information within the time ‘reasonably specified or described’ in the notice (para 7). There is no minimum time limit. Whether the time limit for compliance is ‘reasonable’ will depend on the notice and the information sought.

A person served with an information notice is only required to produce a document if it is in their possession or power (para 18). However, ‘information’ can require the creation of new documents on service of an information notice. And, HMRC is not restricted to asking for documents that it can identify specifically. However, an information notice can only request facts and not opinion. In *R D Utilities Ltd v Revenue and Customs Comrs* [2014] UKFTT 303 (TC), the FTT allowed a company’s appeal against a notice that required ‘subjective’ information.

A frequent area of disagreement is where HMRC requests information contained in ‘non-business’ records, such as private bank accounts. It is sensible to keep personal and business transactions and bank accounts separate. In *Beckwith v Revenue and Customs Comrs* [2012] UKFTT 181 (TC), a number of business transactions had been undertaken through the taxpayer’s personal bank account. The FTT held that his bank statements were business records for the purposes of Sch 36.

# Information notices under Sch 36

## Taxpayer notice (Sch 36 para 1)

HMRC has the power to obtain information and documents for the purpose of checking the taxpayer’s ‘tax position’. This includes future liabilities to pay tax – which allows HMRC to inspect records before a return is filed.

If the taxpayer has already filed a corporation tax or personal self-assessment return for a period, then an HMRC officer cannot issue a taxpayer notice in relation to that period, unless there is an open enquiry, or the HMRC officer has reason to suspect

some non-, under-, or over- assessment.

There is no condition that HMRC ask the taxpayer to provide the information or documents voluntarily before service of a taxpayer notice. There is no obligation on HMRC to obtain prior judicial approval of a taxpayer notice but it can do so. If HMRC has not done this the taxpayer can appeal against the notice.

A taxpayer notice can require the taxpayer to produce documents more than six years old.

## Third party notice (Sch 36, para 2)

An HMRC officer may by written notice to any person require that person to provide information or to produce a document if either is reasonably required for checking the tax position of a known person (a ‘third party notice’).

As with taxpayer notices, third parties can be required to provide ‘information’ by creating new documents. The power is frequently used by HMRC to obtain documents from banks that concern the tax affairs of their customers.

The issue of a third party notice requires judicial approval, unless the taxpayer consents to the issue of the notice. Under FA 2008 Sch 36 para 3(3)(b), the FTT must be satisfied that, in the circumstances, the HMRC officer is justified in issuing a third party notice.

## Judicial approval of taxpayer and third party notices

The FTT will not approve the giving of a taxpayer or third party notice unless it is satisfied that the conditions in FA 2008 Sch 36, para 3(3) are met:

1. The application is made by an authorised HMRC officer.
2. The HMRC officer has reasonable grounds to issue an information notice.
3. A summary of reasons is provided to the taxpayer or third party and the opportunity to make representations has been given.
4. A summary of any representations made has been given to the FTT.
5. In the case of a third party notice, the taxpayer has received a summary of the reasons why the officer requires the information from the third party.

The FTT may disapply requirements 3 to 5 if it is satisfied that taking the specified action might prejudice the assessment or collection of tax. Accordingly, HMRC can obtain a third party notice without prior notice to either the third party or the taxpayer. There is no right of appeal against a tribunal's decision to disapply any of these conditions (Sch 36 para 6(4)).

If the FTT has approved the issue of an information notice, then there is no route of appeal available. The only routes available are judicial review of the FTT's decision to approve the notice; or challenging the imposition of a penalty on the basis that the notice was not lawfully issued.

### Identity unknown notice (Sch 36 para 5)

HMRC can obtain, from a third party, information about a taxpayer or class of taxpayers whose identity is not known; by written notice to any person, requiring that person to provide information.

HMRC may not issue an identity unknown notice to a third party without the approval of the FTT.

An identity unknown notice can be appealed, but the only basis of appeal is that it would be 'unduly onerous' to comply with the notice (Sch 36, para 30). The jurisprudence indicates that 'unduly onerous' is a high bar for the third party to prove.

## The power to inspect premises

FA 2008 Sch 36 Pt 2 introduced a new inspection power. VAT and PAYE inspections habitually involved visits to premises to check records; now inspections can take place in relation to (essentially) all taxes. This power does not give HMRC the right to force entry, or to search. Absent involved third parties, the ambit of the power does not extend to third parties.

### Power to inspect taxpayer's business premises (Sch 36 para 10)

An HMRC officer may enter a person's business premises, and inspect the premises and business assets and business documents on the premises, if the inspection is reasonably required for the purpose of checking that person's tax position.

‘Business premises’ are any premises that an HMRC officer has reason to believe are used in connection with the carrying on of a business by or on behalf of the taxpayer. They include land, buildings, and vehicles.

HMRC cannot review documents that could not have been required to be produced had the occupier been given an information notice at the time of inspection (Sch 36 para 28). In particular, this means that HMRC cannot view documents that are protected by legal professional privilege.

As with information notices, HMRC is not required to obtain judicial approval before conducting an inspection; under Sch 36 para 13(1), an officer may ask the FTT to approve an inspection. There is no appeal to the FTT against an inspection.

HMRC has indicated that, in practice, the time and date of the inspection will be both by negotiation and at the taxpayer’s convenience. Absent agreement, HMRC may carry out an inspection ‘at any reasonable time’ (Sch 36 para 12). Inspections can be made without advance warning (Sch 36 para 12(2)(b)).

A person who deliberately obstructs an HMRC officer in the course of an inspection that has been approved by the FTT is liable to a penalty of £300 and a daily default penalty of £60. There is no penalty if there is a reasonable excuse for the obstruction (Sch 36 paras 39 and 45).

## Restrictions on the use of the powers by HMRC

An information notice only requires a person to produce a document if it is in that person’s ‘possession or power’. Privileged communications are excluded from disclosure. Auditors and tax advisers’ documents are also protected from disclosure.

## Possession or power

Schedule 36, para 18 provides that an information notice only requires a person to produce a document if it is in that person’s ‘possession or power’. This restriction does not apply:

a) to the provision of ‘information’ on service of an information notice; or
b) in respect of HMRC’s power to enter business premises and inspect.

The terms ‘possession’ and ‘power’ are not defined in any of the taxing statutes.

## Possession

‘Possession’ includes ‘custody’, that is, actual physical possession; the right to possession; and ownership.

Documents that are held by an officer or employee of a company will normally be treated as being in the possession of the company (see *Skoye v Bailey* [1971] 1 WWR 144 and *Williams v Ingram* (1900) 16 TLR 451).

## Power

In *Revenue and Customs Comrs v Parissis* [2011] UKFTT 218 (TC) the FTT held that in the context of the taxes acts, ‘power’ should be considered in terms of both legal power and ‘practical’ power. The tribunal indicated that the test as to whether documents are in a person’s power for the purposes of s 20 is whether the person ‘ *can obtain them, by influence or otherwise, and without great expense, from another person even where that person has the legal right to refuse to produce them.’*

## Legal professional privilege

Schedule 36 para 23 provides that an information notice does not require a person to provide information or produce any part of a document which is protected by legal professional privilege.

## Legal advice privilege

Provided that there is a ‘relevant legal context’, a lawyer/client communication will be privileged. There is no requirement that documents protected by legal advice privilege be produced for the ‘dominant purpose’ of legal advice.

Communications between third parties and lawyers or clients are not privileged under this head, even if they are made in connection with the seeking or giving of legal advice.

Communications with other professionals, such as accountants or tax advisers, will not attract legal professional privilege under this head, even if such individuals are

giving advice on legal matters, such as tax law (see *R (on the application of Prudential plc) v Special Commr of Income Tax* [2013] UKSC 1).

## Litigation privilege

Litigation privilege covers communications that came into existence for the dominant purpose of being used in connection with or in contemplation of litigation. There is an overlap between advice and litigation privilege in that, once litigation is in prospect, then lawyer/client documents produced for that litigation will be protected under both heads.

There are two important limits on litigation privilege. First, it does not arise in respect of non-adversarial proceedings. Second, the documents must be produced for the 'dominant purpose' of litigation.

Other documents may, however, be protected by the statutorily created quasi-privileges under Sch 36, paras 19 (documents relating to the conduct of a pending appeal), 24 and 25 (auditors and tax advisers' documents).

## Pending appeals

FA 2008 Sch 36 para 19(1)(a) protects documents 'relating to the conduct of any pending appeal relating to tax' from disclosure under service of an information notice.

Only documents that are brought into existence for the purposes of the preparation and presentation of the appeal are protected (see *Monarch Assurance Co Ltd v Special Comrs* [1986] STC 311). Until an appeal has been made by the taxpayer, para 19(1)(a) does not apply to protect documents, even if prepared for the purpose of contemplated litigation.

## Auditors' and tax advisers' documents

FA 2008 Sch 36 para 24 provides that an auditor cannot be required to provide information held in connection with the performance of carrying out a statutory audit or to produce documents that are his property and that were created in the course of carrying out a statutory audit.

Paragraph 25 provides that a tax adviser cannot be required to produce documents that are his property and which consist of ‘relevant communications’ with his taxpayer client for the purpose of giving or obtaining advice on that client’s tax affairs.

However no protection is provided in relation to information or documents that contain workings showing how a particular entry on the return or accounts was arrived at. And, where the notice relates to an unidentified taxpayer, no protection is provided for such part of a document which contains information as to the identity, or address, of a taxpayer to whom the notice relates.

## Penalties

Failure to comply with an information notice renders the taxpayer liable to a penalty of £300 and an additional £60 for each day on which the failure continues after the day on which the penalty was imposed (Sch 36 paras 39 and 40). A further tax-geared penalty may be imposed for continued failure to comply (Sch 36 para 50). A penalty does not arise if the person satisfies HMRC (or the FTT on appeal) that there is reasonable excuse and, if relevant, the failure is remedied without unreasonable delay after the excuse ceases (Sch 36 para 45).

There is also a penalty for providing inaccurate information pursuant to an information notice. The maximum penalty in relation to inaccurate information is £3,000 (FA 2008 Sch 36 para 40A).

## Conclusion

HMRC possesses extensive powers to obtain information and documents from taxpayers and third parties. Tax advisers in receipt of a third party information notice should objectively assess the strengths and weaknesses of the client’s position, and of HMRC’s position. And if an information request is received and HMRC is alleging criminal conduct, always talk to a lawyer.