

The power of Schedule 36

Beware the pitfalls of an Information Notice, warns Salman Anwar

HMRC has numerous powers to conduct enquiries or make assessments, but the reality is that HMRC requires evidence to come to their conclusions and that evidence comes in the shape of documents and information. The powers contained in Schedule 36 of the Finance Act 2008 are HMRC's primary weapon for evidence gathering. HMRC can demand the evidence from the taxpayer (through a taxpayer notice) or from a third party (through a third party notice), together referred to as 'information notices', but there are strict limitations on what they can demand.

Unfortunately, experience suggests that HMRC often operates on the basis that if you don't ask you don't get, with the result that they may sometimes ask for more than they are entitled to.

If you know the rules you may be able to limit their requests quite substantially – curtailing the length of an enquiry as well as potential costs.

First principles

HMRC can seek documents and information that are in the power and possession of the taxpayer (or a third party) that are reasonably required for the purposes of checking the tax position of a taxpayer. There are many distinct concepts in this statement that we will consider in turn.

What's the difference between documents and information? A document exists but information can be brought into existence. Both can be statutory records (covered later). The definition of documents extends to anything in electronic format and could, for example, include your accounting package.

Possession and power: This is relatively straightforward. Possession means you already have it and power is the ability to obtain it. Your client's historic bank statements may not be in their possession, but it would be in their power to request these from the bank (whether they have retained them is another matter!).

Reasonably required: This can be quite a broad and subjective concept, but the key thing to bear in mind is that the test is for the document or information to be reasonably required for the purposes of checking the taxpayer's tax position. From experience the definition of what HMRC considers to be reasonably required can differ from officer to officer – and may differ from what the Tax Tribunal thinks.

Tax position: Includes past, present and future tax position with regards to most major taxes or duties HMRC has responsibility for – but it is worth bearing in mind that there are separate powers for Customs duties as well as National Minimum/Living Wage. Theoretically, HMRC could ask for details of a transaction before it has completed, although you might be able to challenge the relevance to tax position if you haven't submitted a Return yet. This is an untested area.

Limitations on HMRC

Open enquiry or reasonable suspicion: Where HMRC has an open enquiry the criteria it needs to fulfil to issue an Information Notice are those noted above. However, where it is checking a year that is outside the scope of the statutory enquiry (under S9A or Para 18, for example) then an officer of HMRC needs to demonstrate that they have reason to suspect that there has been an omission/underassessment of some sorts in that period. This is a vague concept but bear in mind that HMRC needs to demonstrate careless or deliberate behaviour (where a return has been submitted) in order to be able to make assessments relating to tax years which fall outside the normal assessment time limits. However, the bar to issuing an Information Notice is only set at reason to suspect.

Old documents: For documents created more than six years ago, at the point the notice is issued, the

agreement of an authorising officer is required.

Legal or litigation privilege: HMRC cannot ask for information relating to the conduct of an appeal, Journalistic material or personal records (as defined in section 12 of POCA 1984) (para 19 of Schedule 36). Similarly, any requests for information of documents that are covered by Legal Professional Privilege (includes Advice and Litigation Privileges) cannot be required by an information notice (para 23 Schedule 36). It is worth bearing in mind that these privileges do not apply to an accountant's legal advice, lawyers must be involved.

Limitation on appeals

Statutory records: The taxpayer has no right of appeal if the documents or information requested is part of a taxpayer's statutory records. While there is no precise definition of what constitutes a person's statutory records, the Taxes Acts define these as the records required to prepare and complete a correct return for a particular year. The Taxes Acts also set out the time limits for keeping such records and if the time limits have lapsed then they are no longer statutory records.

There is also a view that there is a potential to argue that a particular statutory record might not be reasonably required for the purposes of checking a particular aspect of a tax return – so that, for example, the Inspector might not be able to ask for your sales invoices if he is questioning the amount of bank interest you received – although this remains to be tested.

Tribunal approved notice: The taxpayer cannot appeal a notice that has had prior approval from a Tribunal. The only avenue for challenge would be by way of Judicial Review of the Tribunal's decision to approve a notice.

Biggest pitfalls by HMRC

The single biggest category of error we see from HMRC is poor wording of the requests within a notice. Tax cases have concluded that, because a failure to comply with a notice can result in a penalty, it is imperative that the wording must be crystal clear and unambiguous. Note this quote from *Graham Pitcher v HMRC* [2017] UKFTT 406: "When a penalty imposed by the state is under consideration, it is axiomatic that a penalty can only be imposed if it is clear to the citizen exactly what he has to do to avoid the penalty. This is an embodiment of the principle of legal certainty" [emphasis added]

Any notice that uses jargon, short hand or unclear terminology is ripe for challenge and will likely be invalid for the want of clarity. Even the inclusion of one 'etc' can ruin a notice. As an example a request for 'VAT Bad Debt Ledger for the QE 3/18' would likely be too vague and invalid.

Another error made by HMRC is asking for information and documents for a period outside the enquiry period without meeting the above tests.

Biggest pitfall by taxpayers

Failing to appeal the Notice: Not appealing a notice at the outset can severely limit your chances of a successful appeal against a subsequent or later penalty. The leading authority on this subject is the decision in the *PML Accounting Ltd, R (On the Application Of) v Revenue and Customs* [2018] Civ 2231. To analyse this would require an entire article on its own but the key point is to lodge an appeal if you remotely believe there to be inadequacies in the Notice.

Sending in too much: Do not send in more than is required by the notice. For example, if the request is for bank interest details then supply a certificate of bank interest paid – not your statements for the entire year. Likely consequences may be a lengthy enquiry into all your deposits or withdrawals (to the extent where we have seen a taxpayer having to 'prove' that a regular payment to a family member was not the

undisclosed employment of a worker that should have been subjected to PAYE!).

Lastly, HMRC has the power to visit premises, which are similar in nature of the information powers, but that would require a separate article to explain.

Conclusion

Schedule 36 is the biggest weapon in HMRC's armoury. If you know the rules, you might be able to spike their guns and, while that might not end the battle it might put the opposing forces on a more even footing.

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