HMRC is watching you!

Sian Marsden explains how HMRC utilises a wide range of sources to gauge whether the right amount of tax has been paid

HMRC receives lots of information from a wide range of sources to check whether the tax returns submitted by taxpayers are correct. A recent First-tier Tribunal (FTT) case concerning a property investment partnership operated by the taxpayers Mr Davies and Ms Mahil highlighted that HMRC also uses publicly available information to support its compliance activities.

HMRC relied upon details that Mr Davies had included in several books he had written including 'Retire on One Property Deal' and 'Escape the Rat Race with Property Lease Options', and articles featuring quotes by him. These publications claimed net profits of £50,000 and £91,000 on two properties, stated that the couple's five biggest properties were earning profits of £145,000 and claimed that the couple had four holidays abroad totalling six weeks.

HMRC opened an enquiry into their 2017/18 returns to query why the amounts reported on their returns did not correlate with the profits described in his books. HMRC also challenged whether the income declared on their returns was sufficient to support the lifestyles described by Mr Davies. HMRC issued formal Schedule 36 Notices to the taxpayers requesting information and documentation to check the return.

However, a different picture of the business and the lifestyle of the partners emerged during the enquiry.

Although, the partnership had made a £91,000 rental profit on a property, it was reinvested into the purchase and renovation of six other properties on which significant costs were spent, and so the £91,000 profit did not appear on the tax returns. This was the partners' business model and enabled the partnership to expand their property portfolio to 26 properties.

The holidays did take place but were not as lavish as HMRC expected. The couple travelled on budget airlines and stayed in Airbnb accommodation or hostels.

Ms Mahil had also accumulated significant savings by living with her parents, utilising her ISA allowance in full (which does not need to be reported on tax returns) and receiving gifts from her parents. This money helped to fund the couple's day-to-day living and was also invested in their property portfolio.

The FTT found in favour of the taxpayers, and the Schedule 36 Information Notices were deemed not reasonably required. HMRC was clearly asking for further information as part of a 'fishing expedition' when the information presented by the taxpayers showed there was minimal risk of a loss of tax revenues. The Judge also directed HMRC to issue Closure Notices within 90 days of the date of the decision.

Even though HMRC was unsuccessful in this case, it is a timely reminder that HMRC does not just rely on the considerable information it receives from a wide range of sources to check tax returns. Any information in the public domain is available to HMRC too, whether that be in the form of books, articles, social media or even on TV programmes. Those presenting a lavish lifestyle to the media or public, which is not matched by commensurate levels of income on their tax returns, could be opening themselves up to costly, drawn-out enquiries with HMRC.

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