

TAX INVESTIGATIONS AND ENQUIRIES:

NAVIGATING A DISCLOSURE STRATEGY



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During the course of an enquiry or investigation it is common for HMRC to ask for documents and information to help them establish what if any tax is due. Such requests are usually made by HMRC utilising powers made available to them by virtue of the widely drawn legislative provisions found in Schedule 36 FA 2008. Any disclosure exercise whether formal or informal can be emotionally and financially draining for the taxpayer thus it is important to establish the limits to HMRC's powers and the statutory safeguards available to the taxpayer; there may be different avenues to explore over the course of the investigation in relation to the provision of information and it is key to understand the strategic objectives of any disclosure in the context of the specific enquiry sometimes keeping an eye on the end point of what will happen before a tribunal.

HMRC Information Requests

HMRC are not strictly entitled to any information from the taxpayer unless and until a formal request has been made, but a balance between cooperating and not volunteering copious amounts of confidential data in response to an ultra vires request to HMRC must be struck between the taxpayer and HMRC. Inevitably HMRC will at times push the boundaries and try their luck at extracting information that is beyond their remit.

Requests made pursuant to Schedule 36 are limited to seeking information that is reasonably required for the purposes of checking the taxpayer's tax position. The meaning of reasonably required is a point of contention and has been widely debated through the tribunals. The taxpayer must provide documents requested in so far as the information is within their control or easily accessible to the taxpayer.

Physical possession of a document without a right to possession is not sufficient – the taxpayer must have the right to possession of the document. The First-tier Tribunal considers that it is in a taxpayer's power to produce a document if the taxpayer can obtain it by requesting it from another person, even if that person has a legal right

to refuse the request. It is then for the taxpayer to demonstrate that such request to another party would be or already has been denied (HMRC v Parissis & Ors [2011] UKFTT 218 (TC)). The requirement of possession or power applies to documents but does not apply to information (HMRC v Mattu [2021] UKUT 245 (TCC)).

The Tribunal found (obiter) that in the context of the preparation of information for HMRC that there may be a point where the volume of requests become so excessive that the information is not reasonably required (Matharu Delivery Service Ltd v HMRC [2019] UKFTT 553). In several cases, the Tribunal found that the information was not reasonably required because the information or documents sought related to periods outside the normal enquiry window, and HMRC failed to show reasonable, evidence-based grounds to suspect an insufficiency of tax due (see Barty Party Co Ltd v HMRC [2017] UKFTT 697 (TC), Perring v HMRC [2021] UKFTT 110 (TC)). In Ahmed v HMRC [2020] UKFTT 337 (TC), the First-tier Tribunal confirmed that HMRC had the burden of proving that a taxpayer had not complied with a Schedule 36 notice. The unreasonableness of HMRC's requests may also be demonstrated when HMRC persist in asking for more information without good reason, or



when HMRC take an unreasonably long time to process the information provided to them. Note that HMRC may reasonably request information that is contained in non-business records, such as personal bank accounts thus it is always advisable to keep personal and business transaction, as well as bank accounts, separate.

Beyond only providing what is reasonably required, there are other avenues to explore in considering whether or not to deliver requested information- it may be that legal privilege may offer some protection and/or it might be appropriate to apply for a closure notice.



Legal Privilege

Legal professional privilege is a common law rule that protects from disclosure communications between a client and their legal representative who is a legal professional. Legal professional privilege applies to both communications by the client or the legal professional. Privileged material in the possession of a third party is also protected from disclosure.

HMRC cannot use an information notice to require a person to provide privileged information, or to produce any part of a privileged document. Legal professional privilege belongs to the client, and not their legal representative: this means that the client can choose to waive

their right to privilege and provide the information to HMRC. However, when waiving privilege, a person cannot simply cherry pick parts of the advice to disclose as privilege applies to the entirety of the advice. The taxpayer also needs to be careful not to waive privilege inadvertently through their conduct.

There are two types of legal professional privilege: legal advice privilege and legal litigation privilege.

Legal advice privilege applies to documents or information containing confidential communications between a client and their lawyer for the purpose of obtaining or giving legal advice whereas legal litigation privilege applies to documents produced for the dominant purpose of contemplated or actual litigation and advice from lawyers for that purpose. The effect of paragraph 19(1) of Schedule 36 is such that HMRC cannot require a person to provide information or produce a document that relates to the conduct of a pending tax appeal, including in an appeal of an information notice.

It is important to remember that legal advice privilege does not apply to an accountant's advice, such as tax law advice (*Prudential v Pandolfo* [2010] EWCA Civ 1094). However, subject to paragraphs 24, 25 and 26 of Schedule

36, an auditor or anyone appointed to give advice about tax affairs cannot be required to produce documents that are the auditor's property and were created in the course of carrying out a statutory audit or which consist of "relevant communications" with the taxpayer for the purpose of giving or obtaining tax advice.

Closure Notices

When HMRC conclude an enquiry into a tax return, they issue a formal document called a closure notice (section 28A Tax Management Act 1970). Closure notices have traditionally been issued at the end of the enquiry when the taxpayer and HMRC have reached agreement on the tax due. However (following the introduction of partial closure notices ("PCN") by the Finance (No.2) Act 2017) if HMRC's information requests are unreasonable, there has been a rise in taxpayers or their agents making an application to the tax tribunal asking it to direct HMRC to issue a closure notice within a period specified by the Tribunal in an attempt to narrow the scope or limit the parameters of an enquiry to make the disclosure exercise more manageable and "fair".

In an important recent decision, the Court of Appeal (Supreme Court permission to appeal has been denied) in *Embricos v HMRC* [2022] EWCA Civ 3, held that HMRC had no power to issue a PCN in respect of the taxpayer's remittance basis claim, without specifying the tax payable. Having regard to the High Court



decision in *R (Archer) v HMRC* [2016] EWHC 296 the Court of Appeal held that a final closure notice was not valid unless it stated the amount of tax due, and that this principle applied equally to partial closure notices. Note that the question before the court in *Embiricos* was whether the taxpayer's claim for the remittance basis was a matter to which HMRC's domicile enquiry was related. HMRC asserted that a valid PCN would therefore potentially have to state that the remittance basis was disallowed and as a consequence there would need to be amendments made to the self-assessment to bring into charge any relevant foreign income. Mr *Embiricos* was therefore called upon to provide all the details of his worldwide income and gains even though none of it would be taxable unless and until it has been established that the taxpayer had acquired a UK domicile. The result of this decision is to perhaps erode the usefulness of a PCN but certainly to consider very carefully if it is an appropriate tactic to be deployed.



The Disclosure Exercise

Should the enquiry or investigation continue and proceedings are issued, what formed part of any information request quickly becomes the subject matter of the disclosure exercise.

The Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 ("the FTT Rules") contain various provisions regarding the disclosure of documents. In both complex and standard cases, subject to any direction by the Tribunal to the contrary, each party is expected to advise the opponent of the documents on which that party intends to rely or produce, and unless the documents are privileged, to permit the other party to inspect and take copies of them (rule 27). Notably, the provisions in rule 27 do not extend to require a party to disclose documents which are prejudicial to their own case (by contrast, see CPR rule 31.6(b)(i), which requires a party to disclose the documents which adversely affect their own case). Rule 27 also does not have an express requirement to disclose documents referred to in statements of case, witness statements, affidavits, however, a party may ask the Tribunal to make directions which require the other party to disclose documents.

The Tribunal has powers (under rule 5(3)(d) and 16) to direct a party to produce a document to the Tribunal and/or another party. The guiding principle for the Tribunal to exercise such powers is to ask what is required to deal with the case fairly and justly in accordance with the overriding

objective, as stipulated in rule 2(1) (*Addo v Revenue and Customs Commissioners* [2018] UKFTT 530 (TC) applying *Revenue and Customs Commissioners v Ingenious Games LLP* [2014] UKUT 62 (TCC)). Under rules 2(2)(a) and 2(2)(e), dealing with cases fairly and justly includes "dealing with the case in ways which are proportionate to the importance of the case, the complexity of the issues, the anticipated costs and the resources of the parties" and "avoiding delay, so far as compatible with proper consideration of the issues".

Whilst the case of *Addo* concerns disclosure by HMRC to a taxpayer, the decision provides helpful guidance on how the Tribunal approaches the disclosure exercise: the approach is generally broad and will assess the proportionality of a party's request for disclosure, as well as what would be fair and just in the circumstances.

Conclusion

In any tax investigation there is a fine line and delicate tipping point between providing the necessary information and becoming the subject of an unduly onerous fishing expedition. Expert advice will provide invaluable. The decision in *Embiricos* has made it clear that in some circumstances the taxpayer is out of options in resisting the provision of information. There is also a timing argument to consider - comply now or ultimately be compelled to provide information by a court.

