3. Restrictions on HMRC's Schedule 36 powers – "reasonably required"

3.1 Overview

3.1.1 "Reasonably required"

The principal condition for any information notice is that the information or document is for the purposes of checking the taxpayer's tax position or collecting a tax debt (see **2.2.1**). However, this is governed by an overriding requirement that the information or document must be "reasonably required" for such a purpose.

This is an inherently flexible test which allows a tribunal to consider the reasonableness of any particular request by reference to a number of different criteria, principally relevance and proportionality. As confirmed in *Hargreaves*, the test of reasonableness is objective: it is not sufficient for an officer to believe that the information is reasonably required.

This chapter will focus on examples from the case law as to what requests are or are not reasonable in different situations.

Law: FA 2008, Sch. 36, para. 1(1), 2(1), 5(2), 5A(2)
Case: *Hargreaves v HMRC* [2021] UKFTT 80 (TC)

3.1.2 Burden of proof

In early cases, for example *Betts*, it was assumed that HMRC had the burden of proof to demonstrate the reasonableness of each request.

In *Mathew*, however, the tribunal embarked upon a detailed discussion of various authorities and reached the provisional view that, in fact, the burden of proof lies on the taxpayer. Effectively, that provisional conclusion meant that each request is assumed to be valid unless the taxpayer can show that the information or document is not reasonably required.

It is the author's firm view that the tribunal erred in *Mathew*. At the heart of the tribunal's error was its starting point that, generally:

- taxpayers have the burden of proof on statutory appeals to the tribunal; and

- appeals against information notices fall within this category of statutory appeals.

The reason why this represented an error by the tribunal is because most statutory appeals concern challenges to HMRC assessments (or equivalent decisions such as closure notices and determinations). In such cases, the taxpayer is usually seeking a reduction of the amount assessed. However, such proceedings are governed by TMA 1970, s. 50(6), which directs the tribunal to uphold the assessment unless it can be shown that the assessment is excessive. Accordingly, following the usual approach to the burden of proof, it is for the party asserting a particular fact to prove it. If a taxpayer wants an assessment to be reduced, the taxpayer must prove that the assessment is excessive. Section 50, however, has no relevance to appeals against Sch. 36 notices and, therefore, the tribunal in *Mathew* was wrong to rely upon the s. 50 principle by way of analogy.

A further reason why the tribunal misdirected itself in *Mathew* was that the policy behind s. 50(6) is that taxpayers are (theoretically, at least) more likely to have the relevant information so as to allow them to demonstrate any error in the amount assessed. In the context of information notices, however, it is more likely that HMRC (rather than the recipient) will have the information that will allow the tribunal to determine the reasonableness of any particular request.

Finally, the tribunal in *Mathew* failed to apply the fundamental principle that it is for the party asserting any particular fact to prove it. In the context of Sch. 36 notices, HMRC are implicitly asserting that what they are asking for is reasonably required. Accordingly, this is something that they must prove.

The matter was then fully reviewed by the tribunal in *Cliftonville*, which concluded that the burden is on HMRC to show that information requests are reasonable.

Later cases have generally proceeded on that basis. Indeed, in *Duncan*, the tribunal (which comprised the same judge whose view in *Mathew* was that the burden of proof in Sch. 36 notice cases fell on the appellant) recognised that the analysis in *Cliftonville* was "careful".

It is the author's experience that HMRC now generally accept that they have the burden of proof to show that the "reasonably required"

test is satisfied. However, occasionally, they point to the *Mathew* case to give the impression that the matter is not beyond doubt. Indeed, in *Perring*, HMRC once again asserted that the burden of proof fell on the taxpayer. The tribunal reconsidered the matter afresh, concluding that the burden fell on HMRC.

It will, of course, be remembered that decisions of the tribunal are not binding and this permits judges to look at matters afresh each time. Furthermore, as noted at **10.3.4**, a decision of the FTT in an appeal against a Sch. 36 notice may not itself be the subject of appeal to the Upper Tribunal, meaning that there is a dearth of binding precedent to guide the FTT. Nevertheless, the author has observed that the FTT now seems to accept more readily that the burden of proof does indeed fall on HMRC.

On the other hand, the decision of the FTT in *Perlman* could be interpreted as suggesting that any factual determination by HMRC that underlies a decision to issue a Sch. 36 notice may not be challenged on appeal by the recipient, except in cases where it can be shown that HMRC's factual determination is unreasonable.

As discussed at **13.9.4**, the author respectfully considers that the FTT went astray in that case. Furthermore, the *Perlman* case concerns a domicile dispute where some confusion has reigned in a number of other cases. Even if *Perlman* represents good law in the context of domicile disputes, the author does not expect the FTT to extend the *Perlman* approach to appeals more generally.

Cases: *Mathew v HMRC* [2015] UKFTT 139 (TC); *Cliftonville Consultancy Ltd v HMRC* [2018] UKFTT 231 (TC); *Duncan v HMRC* [2018] UKFTT 296 (TC); *Perring v HMRC* [2021] UKFTT 110 (TC); *Perlman v HMRC* [2021] UKFTT 219 (TC)

3.2 Reasonably required

3.2.1 Overview

The "reasonably required" wording is deliberately vague so as to allow it to be applied flexibly in a wide range of cases. As the tribunal said in *Holmes*:

> "Schedule 36 imposes a test of reasonableness in relation to the documents and information that taxpayers can be required to provide. In my view it is not possible to lay down any general

> rule as to what will be considered to be reasonable in enquiries generally. What is reasonable will depend on all the circumstances of the case."

In *Uppercut*, the tribunal emphasised that the scope of any particular investigation is a relevant consideration when determining what is reasonably required. For example, if the factual evidence suggests that HMRC are carrying out a corporation tax investigation, a document cannot be reasonably required if it is relevant only to the taxpayer's VAT position.

A commonly arising question relates to the provision of private bank statements. That is addressed at **3.3**.

A range of other scenarios is set out at **3.4**.

Cases: *Uppercut Films Ltd v HMRC* [2018] UKFTT 232 (TC); *Holmes v HMRC* [2018] UKFTT 678 (TC)

3.2.2 What makes information "reasonably required"?

One of the practical difficulties in any HMRC investigation is that an officer is supposedly in a position of ignorance at the start of the process and it is in order to overcome that ignorance that the officer requests information or documents. Accordingly, although the burden of proof is on HMRC to demonstrate the reasonableness of any request, this is likely to be easily discharged in many cases. As the tribunal held in *Perfectos*:

> "… these appeals very clearly highlight the balance that must be struck between giving [HMRC] sufficient latitude in relation to their information and enquiry powers so as to allow them to properly do their jobs and the taxpayer's right to finality and privacy."

On the other hand, as that balancing exercise implies, explanations from the taxpayer as to why something is not reasonably required must be taken into account.

Example 1 – Josh Ltd

In its 2021 accounts, Josh Ltd shows entertaining expenditure of £25,000, none of which was added back. In the course of an enquiry, HMRC determine that the expenditure all related to client

entertaining and, therefore, the expenditure was wrongly claimed as an allowable expense.

On the basis of this error in the 2021 accounts, HMRC seek a breakdown of the entertaining expenditure incurred by the company in its 2017, 2018, 2019 and 2020 accounts.

At this stage in the process, it is arguable that the information sought by HMRC is reasonably required.

However, that might not be the case if, for example, the company reminds HMRC that all entertaining expenditure was in fact added back in the earlier years and, accordingly, it is unnecessary for this information to be provided.

The following is a more nuanced example.

Example 2 – Geetha Ltd

The facts of Geetha Ltd are the same as those of Josh Ltd in Example 1 so far as the 2021 accounts are concerned.

However, the reason for the error in that year's tax return is attributed to a change in its advisers/personnel.

In those circumstances, Geetha Ltd might be able to argue that this fact is sufficient to explain why an error occurred in one year and therefore makes any investigation into earlier years axiomatically unreasonable.

In the author's view, Geetha Ltd's explanations are probably insufficient to defeat the request on the basis of the "reasonably required" test. However, assuming that there is no valid enquiry into the earlier years' returns, the company would be more likely to succeed in relation to the Condition B test ("reason to suspect") – see **2.4.4** and **2.4.5**.

From a practical perspective, the author would suggest that Geetha Ltd complied with HMRC's request so far as 2020 is concerned (so as to demonstrate adherence to the rules on entertaining expenditure). Compliance in that one year would then be likely to defeat any argument that HMRC have reason to suspect an under-assessment in the earlier years.