

Mark Morton @ Mervin-group-co.uk

A very private affair

MARK MORTON discusses HMRC's right to demand access to a taxpayer's private bank account.

As I sat ploughing my way through the 600,000 or so denoted web pages of HMRC's *Compliance Handbook* in a spare half hour, I came across an interesting omission: CH223430 had disappeared.

This section had originally been in the *Enquiry Manual* 2221 for almost a decade. When the *Compliance Handbook* was written, EM2221 was cut and pasted into CH223430 almost unchanged. Intriguingly, EM221 can still be viewed at www.hmrc.gov.uk/manuals/emmanual/EM2221.htm.

What's the problem?

Ever since the self assessment enquiry regime came into being, it has been a moot point whether or not HMRC can demand access to private bank accounts. The new information powers at FA 2008, Sch 36 have not really clarified this issue. Schedule 36 gives HMRC an unappealable right to demand 'statutory records'. Statutory records are the documents and information which a person is required to keep and preserve to fulfil their obligations under the Taxes Acts and VAT legislation.

The new information powers contain no more detailed requirements, so we have to go back to TMA 1970, s 12B to see what this might mean to an individual.

Taxpayers must retain records which substantiate the entries on the return. Broadly, a business taxpayer is required to maintain records of:

- receipts and expenses;
- sales and purchases;
- other supporting documents.

for five years after the fixed filing date.

KEY POINTS

- Disappearing guidance in HMRC's *Compliance Handbook*.
- Are private bank account details statutory records?
- Right to see statutory records, FA 2008, Sch 36.
- Too many unsubstantiated demands for private bank account records.



Note that a business taxpayer's return may also include private bank accounts, etc. The legislation talks of 'records kept by a business taxpayer', not 'business records'. Therefore, private bank details would be caught by this five-year rule.

Non-business taxpayers have to retain records to substantiate entries on the return for one year from the fixed filing date. So, in respect of a purely private bank account, the only entry on the return which would have to be substantiated is the interest figure.

Interestingly, purely private bank statements are clearly not statutory records and so the taxpayer is not obliged to keep them at all.

What was the guidance?

The missing guidance in *Compliance Handbook* CH223430 stated:

'The over-riding test is based on what is reasonable (that is, fair and sensible) in the circumstances. The question of whether it is reasonable to request private documents including bank and building society accounts can only be determined by reference to the facts in each individual case.'

'Non-business bank details should not be requested in the opening letter as a matter of course. However, where accounts are not based on a robust and effectively operated record keeping system which is supported by adequate and appropriate safeguards and/or include unvouched or unverified sums, it would be reasonable to request the private bank details with the other records. The position could be established through telephone contact with the agent or by making the basis of the request clear in the opening letter.'

The manual went on to cite some examples where inspectors might want to see private bank records:

- they think that undeclared income or gains have been credited to the private account;
- they have doubts or questions about means or capital growth;
- they think that the tax return was based, wholly or partly, on the 'private' bank account documents;
- where taxable receipts or expenditure are unvouched or estimated and it is reasonable to expect that this expenditure should have been vouched/recorded; or
- where payments from an account to the business are treated as non-taxable, for example capital introduced (where not independently verified).

The manual then states:

'When determining whether to require non-business information you should consider

- 'costs (in time and money), and pursue the matter only where you are satisfied that the potential benefit to the check is proportionate to these costs. This is particularly relevant in seeking duplicate statements for non-business bank accounts;
- 'rights of privacy (Article 8). You should pursue the matter only where you can demonstrate that the information or documents to be required are an effective way of dealing with the queries we have about the tax returns and the intrusion into the person's private life is the minimum necessary to achieve this aim.'

Practical implications

It is worth bearing in mind how HMRC should operate an enquiry, particularly into a business. They are supposed to make a case, on the balance of probabilities, that the business records are 'materially inaccurate' (my terminology). To use an HMRC phrase, the records have to be 'broken'.

Once that has been done, HMRC are then at liberty to try to quantify the omissions. If the omissions are extractive, this could entail a business economics exercise, a means test or a capital statement. All of these are meaningless, however, unless the records have been broken in the first place.

What is clearly unacceptable is to demand the private bank accounts at the outset of an enquiry, demand explanations of every private transaction and state that, if each private transaction cannot be explained, those deposits will be taxable. Yet this is exactly the approach I have seen regularly in the last few months.

The HMRC guidance clearly makes the following points:

- requests have to be reasonable (fair, sensible, proportionate, not excessive, suitable, logical);
- the records have to be broken;

- non-business bank details should not be requested in the opening letter as a matter of course;
- costs: copies of private accounts should only be demanded if the cost to the taxpayer is proportionate to the risk; and
- Article 8 of the Human Rights Act gives individuals a fundamental right to privacy in their private affairs unless they have been fiddling their tax, but HMRC have to make a case that the taxpayer has been fiddling.

The real world

It is interesting currently that there are so few enquiries about. However, those in existence seem almost to be following a pro forma approach: 90% of the requests are standard and every 'new style' enquiry that I have come across requests private bank accounts in the opening letter, clearly contradicting the missing guidance in CH223430.

In the most recent case that I have seen, HMRC requested all the business records, etc., but wanted an initial meeting with the taxpayer to discuss the way the business operated and also the private affairs of the proprietor. At the meeting, HMRC focused purely on the private affairs, 'interrogated' the taxpayer and demanded the private accounts.

“At the meeting, HMRC focused purely on the private affairs.”

Three months down the line, the taxpayer has received an information notice demanding verification of numerous private transactions, copy statements, credit card statements and mortgage application form. HMRC have not even looked at the business records yet.

As to how this could affect you, here is an example. I bought three test match tickets for Trent Bridge last October on my credit card. I received two cheques from the other two attendees to reimburse me and banked these accordingly. If, at a later stage, I could not explain these deposits, HMRC might say that they are omitted takings, regardless of the fact that they would have proved no tax offence had been committed – just a bad memory on my part.

Where does this leave us?

The guidance in CH223430 has currently been replaced with nothing. It is not clear why it has disappeared but the principles contained in it are not new and, even without guidance, the moral is clear: no access to private bank accounts unless HMRC prove, on balance, there's a fiddle. ■

Mark Morton is head of tax at Mercia Group Ltd, one of the UK's largest providers of training and support services to the accountancy profession. He can be contacted on 0116 258 1200.