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Professional Conduct in Relation to Taxation

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PROFESSIONAL CONDUCT IN RELATION TO TAXATION

Guidelines issued in October 1997 revised for self assessment

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I INTRODUCTION

1. PRELIMINARY

Basis of guidelines

1.1 These guidelines have been prepared in conjunction with the Institute of Chartered Accountants in England and Wales and the Institute of Indirect Taxation. Sections 2 to 8 have been reviewed by the Revenue and sections 2 and 9 to 11 have been reviewed by Customs. Whilst not necessarily agreeing with every view expressed the Revenue and Customs acknowledge that these sections are an acceptable basis for dealings between members and the Departments.

1.2 Since their issue in November 1995 the guidelines have been reviewed and amended so as to include self-assessment. In particular, new Sections 4 and 7 and new Annexes C and H have been added. The guidelines explain how self-assessment impacts on professional conduct; they do not represent an exposition of how self-assessment works.

1.3 In following these guidelines it should particularly be borne in mind that each case depends upon its own circumstances and if a member is in doubt, he should seek advice from the Institute and, where appropriate, independent legal advice.

1.4 Section 3 and Annexes A (updated for self-assessment), B, and D to F of these guidelines (Disclosure to the Inland Revenue) represent substantially the document issued jointly by the Chartered Institute of Taxation and the Institute of Chartered Accountants in England and Wales in February 1992.

1.5 Section 6 of these guidelines (Inland Revenue errors) represents substantially the text of a statement issued by the Chartered Institute of Taxation in March 1993.

Interpretation

1.6 In this statement "client" includes where the context requires "former client". "Member" (and "members") includes "firm" or "practice" and the staff thereof. "The Revenue" means the Inland Revenue, "Customs" means H M Customs and Excise and "tax authorities" means either or both as appropriate. The masculine gender imports the feminine gender throughout this document.

Abbreviations

1.7 The following abbreviations have been used:

CEMA 1979	Customs and Excise Management Act 1979
FA	Finance Act
TA 1988	Income and Corporation Taxes Act 1988
TCGA 1992	Taxation of Chargeable Gains Act 1992
TMA 1970	Taxes Management Act 1970
SI	Statutory Instrument
SP	Statement of Practice
VATA 1994	Value Added Tax Act 1994

2. PRINCIPLES APPLICABLE TO ALL TAXES

Generally

2.1 The proper functioning of the UK tax system depends very heavily on mutual trust between the tax authorities and members of the Institute. Thus, members should ensure that their dealings with the tax authorities are such that the officer can appreciate what position is being taken by the taxpayer and can make such further enquiries as he may consider to be necessary. The following guidance is equally applicable to an assessment and a self-assessment taxation regime.

Relationship with the client

2.2 In dealing with a client's taxation affairs a member's role is often that of agent but he may be acting as principal in an advisory capacity. The contractual relationship should be governed by an appropriate letter of engagement in order that the scope of both the member's and the client's responsibilities are made clear. For reasons explained elsewhere in these guidelines (see in particular paragraph 5.22) members are urged to include in the letter of engagement a statement to the following effect:

> "We will observe the ethical guidelines of our professional Institute and accept instructions to act for you on the basis that we will act in accordance with those guidelines. In particular you give us authority to correct Inland Revenue errors.".

Members should refer to the separate guidance note issued in October 1997: "Engagement letters for tax practitioners".

2.3 Every relationship should be covered; if the member acts for a partnership and also for one or more of the partners, then the partnership and each partner acted for are separate clients for the purposes of this statement. Likewise, if the member acts for a husband and wife, each is a separate client.

2.4 If the client is a body corporate the client is the company and not the directors. Where a default of any kind is discovered, the matter should be raised at the appropriate level in the client organisation. Where the directors' actions have resulted in the company's defrauding the Crown, references in the statement to the "client" should be regarded in the first instance as referring to the directors. For example, where the member has to advise a client to make a full disclosure to the tax authorities, the advice should be addressed to the directors. If it is believed that this advice will not be brought to the attention of the board as a whole, it should be given to each director, and then, if appropriate, to shareholders. Where the member is also the auditor it may be appropriate to cover this in the audit report.

2.5 A member should deal with taxation work only on the basis of full disclosure by the client. Such disclosures are governed by confidentiality as an implied contractual term.

2.6 These guidelines explain the position of members if a client refuses to act in accordance with the member's advice, for example where the client has unreasonably delayed either the production of information needed for the preparation of returns or accounts or the full disclosure of irregularities. The member should consider whether to continue to act for the client but should note the recommendation contained in Sections 5 and 10 regarding termination of relationships with the client.

2.7 If a member believes that a relationship with a client has been or is likely to be terminated, whether by the client or by the member, the member needs to take extra care to make clear to the client in writing what matters within the terms of the engagement have been dealt with and what remains to be done, and by what date it should be done, and also what further action the member will, or will not, take.

2.8 Members may find it additionally helpful to refer to section 1.306 (Professional conduct in relation to defaults or unlawful acts) of the Institute of Chartered Accountants in England and Wales Members' Handbook. Paragraphs 3 (full disclosure), 7 (confidentiality) and 13 to 21 (as regards freedom to disclose) are particularly relevant. Members who have any difficulty in accessing this information should contact the Deputy Secretary of the Chartered Institute of Taxation.

Tax avoidance

2.9 Tax avoidance is legal and is to be distinguished from evasion which is illegal. All taxpayers have the right to arrange their affairs under the law to minimise their liability to tax. The member should consider carefully the merits of arrangements which may be considered artificial by the tax authority concerned. Such schemes may not be in the client's wider interests because of the risk that they may be challenged by the tax authorities.

2.10 The tax authorities say that they object to arrangements set up for no purpose other than to avoid tax. They see such artificial arrangements as fundamentally different from choosing one commercial option, which generates a lower tax bill than another, or the mere organisation of a taxpayer's affairs in such a way as to minimize the tax bill.

Disclosure

2.11 In all tax matters, the member must act in good faith in dealings with the tax authorities, in particular the member must take care when making statements or asserting facts on behalf of a client. However, the member's duty to try to ensure that the information provided is accurate and that relevant facts are not withheld is not always simple to achieve, especially if the client does not co-operate. See Sections 3 and 4 (direct tax) and 9 (indirect tax).

Files and working papers

2.12 Members should keep copies of returns etc. and organise their working papers to separate matters such as the preparation of accounts and tax returns from those on which audit and other opinions may be expressed, because the latter are normally protected from disclosure. See paragraph 2.19 and Annex I, paragraph 7.

Members in practice overseas

2.13 Members in practice overseas are required to comply with local laws. They should follow the guidance of the Institute unless well-established and generally-accepted practice of local firms is to the contrary.

Responses to official requests

2.14 A member who is asked by the tax authorities to disclose documents should:

(a) contact the client;

(b) not give the tax authorities unfettered access to working papers without taking advice, if necessary, as to which papers the tax authorities are entitled to see and which parts of appropriate papers the member is obliged to disclose; and

(c) separate disclosable papers from others.

Where the member has ceased to act the enquirer should be referred to the former client.

2.15 Generally, advice given by a member to his client is not disclosable by the member to the tax authorities. As regards Revenue taxes only, an inspector may, under certain conditions, require documents in a member's possession or power relevant to tax liabilities: TMA 1970 s.20(3). However, this excludes documents which are the property of a member and were either created in relation to certain audit functions or relate to tax advice: TMA 1970 s.20B(9), (10). See also Annex I (Inland Revenue's powers to obtain information) and Annex K (Customs' powers to obtain information). As to ownership of documents, when in doubt the member may wish to take legal advice.

2.16 The member should also consider whether the tax authorities are able to obtain the information they need from some other source and can be told accordingly.

Legal professional privilege

2.17 Legal professional privilege is related to but not quite the same as the general duty of confidentiality owed to a client (as to which see paragraphs 3.25 to 3.27 below). Legal professional privilege, a part of the common law, has been developed and normally applies in the context of court proceedings, civil or criminal, where it can operate to exclude privileged material from having to be disclosed to the other party or, if known to the other party, being brought into evidence by him. Even if a document is privileged at common law a further question arises in the tax context: does the common law privilege justify a refusal to disclose the document to the Revenue? This is discussed in paragraphs 2.20 and 2.21 below.

2.18 At common law the concept of legal professional privilege is complex. The protection it provides has significant limitations. It is not the case that every communication, of whatever nature, by or to a lawyer (barrister, Scottish advocate, or solicitor) is privileged. At common law the two significant situations in which privilege arises are as follows:

(a) *Litigation privilege.* Documents created for the dominant purpose of litigation are privileged. The privilege covers not only documents prepared by the lawyer, but also documents brought into existence by third persons for the purposes of litigation. Therefore, once litigation has started or is contemplated, documents prepared by non-lawyer advisers (including tax advisers) may be privileged. It is considered that litigation for this purpose includes a tax appeal, although there appears to be no case in which this point has been expressly confirmed.

(b) *Advice privilege.* Documents passing between a client and his legal advisers are privileged if they are written for the purpose of obtaining or giving legal advice. Who is a legal adviser for this purpose is an open point, but the description is not restricted to lawyers in private practice. This type of privilege does not extend to documents to or from non-lawyers. So tax advice (not obtained for purposes of litigation) from a non-lawyer adviser is not privileged at common law. Nor are commissioned reports or investigations of companies.

2.19 Legal professional privilege should not be confused with the protections from disclosure to the Revenue given to tax advisers by some subsections of TMA 1970 s.20B (see further paragraph 2.15 above). These latter protections arise from express statutory provisions and are protections of the adviser - restricting the powers of the Revenue to require information or documents from him. Legal professional privilege, on the other hand, exists under the common law and is the privilege, not of the lawyer, but of the lawyer's client. The general common law rule is that the client, unless he waives the privilege, cannot be required to produce documents or answer questions where the subject matter is protected by privilege; nor can the lawyer produce the documents or answer the questions without the client's consent. There are exceptions, one of which is where a document came into existence as a step in criminal or illegal activity. It is immaterial whether the member was a party to the criminality or illegality.

2.20 Another possible exception is where the common law privilege is overridden by an express statutory provision. In this connection unclear questions may arise in the tax context. In particular, are documents or information which are covered by common law privilege protected from disclosure pursuant to a statutory notice (for example under TMA 1970 s.20) served on the client or the member? Or is the correct legal position that a valid statutory notice overrides privilege at common law?

2.21 There is little or no guidance on these questions in reported cases. It is, however, not uncommon for members, or their clients, when asked for some particular document or item of information by the tax authorities, to reply to the effect that, because the document or information is privileged, it is not being disclosed. If a member is consulted about, or receives himself, a request from the tax authorities (whether in the form of statutory notice or not) which calls for disclosure of material which he believes to be privileged at common law and which the client does not agree to disclose, it is suggested that in the first instance the member should reply along the lines mentioned. (See also paragraph 2.14) The tax authorities may not pursue the matter: frequently they do not (though this should not be regarded as some sort of tacit acceptance on their part that privileged matters are as a matter of law protected from compulsory disclosure under statutory powers). If they press the request for the documents or information it will probably be sensible for the member to seek specific legal advice.

Irregularities

2.22 In the course of a member's relationship with the client, whether as agent or principal, he may become aware of irregularities committed by the client. If something is amiss, the client should be informed at once, normally in writing. Tact may be required and immediate corrective action may be difficult but the member should be seen to have acted correctly at the outset.

Materiality

2.23 The concept of materiality is not recognised by the tax authorities in enforcing the tax legislation, and the fact that an error is a small amount does not of itself mean that a member can ignore it.

2.24 In considering whether to cease to act because a client refuses to make some particular disclosure to the tax authorities, a member may have regard to the materiality of the amount involved in relation to the total tax liability. The member is entitled to take the view that he is not obliged to cease to act where the amount is not material.

2.25 See paragraph 6.2 for comments concerning Revenue errors and Sections 5 and 10 dealing with acquiring knowledge of direct tax and VAT irregularities respectively where the concept of materiality arises.

2.26 The "materiality" of an amount is a matter to be decided on the member's judgement in relation to each particular case. An amount which is not material in the conduct of an audit may be material for tax purposes.

Money laundering

2.27 Under the terms of the Criminal Justice Act 1993, tax evasion amounting to an indictable offence, or equivalent conduct overseas, will result in the acquisition of criminal proceeds. Under a strict interpretation of the legislation this amounts to money laundering and could require a report to be made to the National Criminal Intelligence Service (NCIS). Although there is no specific offence of failure to report money laundering other than that relating to drugs or terrorist activities, members should consider reporting any suspicions they have formed as a defence to a possible charge of assisting a money launderer. In particular, where a client has refused to disclose an admitted irregularity, or where criminal conduct, separate from or in addition to the tax evasion, is suspected, a report may be appropriate.

2.28 Firms engaged in relevant financial business as defined by the Money Laundering Regulations including those authorised under the Financial Services Act for the provision of investment services, are required to establish procedures for the forestalling and prevention of money laundering, including the reporting of money- laundering suspicions. Many other firms are expected to have established such procedures as a matter of best practice, or because services likely to be of use to a money launderer may be provided. Members should normally report through their firm's usual procedures.

2.29 A report by a member to NCIS may be used in furtherance of criminal enquiries. NCIS have stated that information will not be passed to the Revenue, or otherwise be passed on in the furtherance of tax collection. A report to NCIS should therefore not be considered a substitute for proper disclosure to the tax authorities. Where a report has been made to NCIS, the client should not normally be informed since this may amount to "tipping-off" under the terms of the legislation.

2.30 The money-laundering legislation does not prevent a member from advising clients on negotiations with the tax authorities in respect of evaded tax liabilities, on a bona fide basis of full disclosure in accordance with this Statement.

II INLAND REVENUE TAXES

3. DISCLOSURE TO THE INLAND REVENUE

Introduction

3.1 In recent years, the Revenue's expectations of the role and responsibilities of members when preparing tax returns and computations and when corresponding with the Revenue have differed in certain respects from common practice, which itself has not been entirely consistent. These guidelines provide advice to members on how to take reasonable steps to ensure that their clients meet all the requirements of revenue law and practice in relation to the disclosure and presentation of information in tax returns, computations and related correspondence with the Revenue. Further guidance in relation to self-assessment is given in Section 4.

3.2 Although these guidelines refer to such matters as "discovery" (the right of the Revenue to reopen previously-agreed assessments or to make further assessments) and the deliberate withholding of information by taxpayers, they are not covered exhaustively.

3.3 Disclosure is a complex subject. Statute law provides little guidance. Case law, notably *Cenlon Finance Co. Ltd v Ellwood (HL 1962 40 TC 176), Olin Energy Systems Ltd v Scorer (HL(1985) 58 TC 592) ("the Olin Energy decision"), and R v CIR (ex parte Matrix Securities Ltd (HL 1994, TL 3396)),* has assisted to some extent but there are significant differences in the interpretation of some of the case law as between the Revenue and the professions. (See also paragraph 3.32).

3.4 A member who submits a tax return or tax computations for a taxpayer is acting as an agent. This has an important bearing on his responsibilities.

3.5 Conflicts can arise between a member's duties to his client, his obligations under statute and his understanding of "best practice" in dealing with the Revenue. One purpose of these guidelines is to help him resolve those conflicts. These guidelines do not purport to cover every conceivable combination of circumstances which may arise and they are not an exhaustive set of rules which can be used to justify a particular course of action by taking individual paragraphs or sentences out of context, or because a particular issue is not specifically covered. Nevertheless, the guidelines should help members in their day-to-day dealings with the Revenue, although many judgemental decisions will remain and the final determination will depend on the precise circumstances of the particular client. It should, however, have regard to these guidelines.

Relevance of disclosure provisions

3.6 It is important to ensure, as far as it is possible and reasonable to do so, that

(a) the taxpayer has satisfied the statutory reporting requirements, namely that the return is to the best of the taxpayer's knowledge correct and complete;

(b) the Revenue cannot successfully contend that there has been fraudulent or negligent conduct; and

(c) the Revenue cannot subsequently make a discovery and hence reopen previously-agreed figures or positions.

Further details and comments on the relevant statute law are set out in Annex A.

3.7 Whether or not a particular matter or figure should be disclosed to the Revenue falls broadly into one of four categories:

(a) there is a clear legal obligation to disclose; or

(b) there is a possible legal obligation to disclose, but the matter is not free from doubt (for example where the member is uncertain whether tax is chargeable or an expense is allowable). These "grey" areas vary by degree. The member will have to make a professional judgement, based on his knowledge of all the facts and circumstances. A member will wish to be satisfied that any decision that disclosure is not needed is well founded. Further guidance on this issue is set out below; or

(c) there is no legal obligation to disclose, but the member concludes that there are valid reasons for making a voluntary disclosure or recommending to a client that voluntary disclosure be made for example prudence or where Revenue practice is known (see paragraphs 3.54 to 3.58); or

(d) there is neither a legal obligation to disclose nor any valid reason to make a voluntary disclosure.

3.8 These guidelines do not include a comprehensive review of the civil and criminal aspects of tax defaults, namely fraudulent conduct, negligent conduct, failures and errors. Nor do they consider the interaction with the concept of professional negligence. However, Annex B and Annex C review some of the civil aspects of tax defaults for pre self-assessment and self-assessment respectively. The consequences of fraudulent conduct are not limited to the TMA 1970 and can arise under the general criminal law. Annex D gives brief particulars of some of the criminal aspects of tax defaults.

Areas of doubt

3.9 The Keith Committee Report on the Enforcement Powers of the Revenue Departments recommended that the taxpayer should be required to give the Revenue details of any items (of income, profits or costs or expenses) where the taxpayer had "taken the benefit of any doubt". That recommendation was heavily criticised by a number of commentators, largely on the grounds that it was burdensome and inequitable and would be unworkable in practice. During the parliamentary debates on the 1989 Finance Bill, the Government announced that they had accepted that criticism and did not propose to introduce such a disclosure requirement. However, where there is a genuine doubt on an issue, it is unlikely that the requirement to make a complete and correct return would be met unless appropriate disclosure has been made.

3.10 The final decision on the manner of disclosure, if any, rests with the taxpayer. To enable clients to make such decisions, a member should take reasonable steps to ensure that the taxpayer receives advice either from the member or other advisers with relevant experience and expertise.

3.11 Even where the taxpayer has sought advice from another adviser, a proper evaluation will have to be made of the standing of that adviser and the strength of his opinion. Normally, members should help their clients with such evaluations.

3.12 In considering what information ought to be disclosed to the Revenue, account must be taken of:

(a) the exact terms of the legislation (for example apparently independent transactions which are in fact disposals of a set of articles within TCGA 1992 s.262(4);

(b) the strength of any argument that the substance and true nature of a series of transactions can be ascertained only if the transactions are considered as a whole (for example where there is a preordained series of transactions);

(c) the best interests of the taxpayer, having regard to all the taxpayer's actual or expected dealings with the Revenue, past, current and future, even though there is no legal obligation to disclose (for example receipt of a substantial legacy which has given rise to new sources of income); and

(d) the need to avoid repetition of work and the incurring of unnecessary costs: some aspects of this subject are considered further in paragraphs 3.38 to 3.43.

3.13 If, having regard to these guidelines (particularly those in paragraphs 3.9 and 3.50 to 3.53), a member is satisfied that a particular source of income, profits or gains is not taxable, there is no legal requirement for it to be reported. Similarly, where a member is satisfied that an expense included in a profit and loss account is allowable, separate disclosure of that item is not necessary unless specifically required by law, or in response to a specific Revenue enquiry.

3.14 Where a member believes that an expense is disallowable, it would be wrong for the member to claim it is allowable on the basis that the Revenue may not, for example, ask for any analysis of the expense account in which the item in question is included.

3.15 Where a proper analysis is given in an accompanying schedule, an expense should not be claimed where there is no valid technical ground for such a claim, unless there is reason to believe that the Revenue would grant it in practice in which event the item in question should be specifically highlighted, for example in the letter to the inspector enclosing the computations. Claims should not be made on the basis that the Revenue may allow them by default.

3.16 Normally, there is no advantage in disclosing more than is required by law, especially if to do so involves additional expense. However, it may sometimes be advantageous to report a particular matter or figure in the hope of avoiding inconvenient or detailed and time-consuming Revenue enquiries in the future.

3.17 Particular care is needed where the member believes that the taxpayer's treatment is correct but in the member's experience:

(a) the Revenue will request the relevant figures or information if not shown voluntarily (for example as required by form CT 200); or

(b) the Revenue are likely to seek to challenge that treatment. (See also the comments in paragraph 3.56.)

3.18 A member who is uncertain whether to disclose a particular item should consider taking further advice before reaching a decision, notably from a more experienced member, from a specialist on that subject, or from counsel. If the member then concludes that no disclosure is necessary, he should record the reasons.

3.19 Such decisions may have to be justified at a later date, so the files should contain sufficient evidence to support the position taken, including copies of any second opinion obtained and notes of discussions with the client or with other advisers.

3.20 In difficult cases, where the member is the agent of the client, and is satisfied that no disclosure is needed (or that disclosure is appropriate, for example, on the grounds of prudence), the member should take reasonable steps to ensure that the client understands the issues and implications and the proposed course of action. The member's files should record the fact that such discussions took place with the client and the client's final decision.

Discovery

3.21 Case law indicates that, unless the decision in the *Olin Energy* case applies, the Revenue can make a "discovery", even though the taxpayer has satisfied the statutory reporting obligations (and hence the Revenue could not successfully contend that there has been fraudulent or negligent conduct) and figures have been agreed.

3.22 The law on "discovery" is complex. In principle, the Revenue take the view that they are empowered to make further assessments following discovery of an under assessment. The expression "discovers" has been held to be synonymous with `finds out'. It can include a change of mind about the same set of facts or about the law.

3.23 The Revenue views in the light of the *Olin Energy* decision were published as SP8/91 (see Annex E).

Practical considerations

3.24 A member who prepares a tax return or tax computations for the client's approval acts for the client, and thus has a duty to present the client's position to the Revenue in the most advantageous manner within the law and having regard to these guidelines. That same duty arises where a member is involved in correspondence with the Revenue on behalf of the client. In all cases the client's position should be presented in a way which is factually correct and is not intended to mislead an ordinarily competent inspector.

3.25 A member owes a duty of confidentiality to the client. Thus, in general, a member cannot disclose any information received in a professional capacity, without the consent of the client whether contained in the engagement letter or elsewhere.

3.26 However, if a client refuses to accept the advice of a member in circumstances where the member believes that disclosure should be made, the member should consider whether he can properly continue to act for that client in relation to the return or computations in question and for the client generally.

3.27 The case of *Tournier* v *National Provincial and Union Bank of England ([1924] 1KB 461)* established that the normal duty of confidentiality may be overridden in certain circumstances, notably:

(a) where disclosure is legally required (for example where a member receives a notice under TMA 1970 s.20(3) unless the documents are protected by TMA 1970 s.20B); or

(b) where there is a duty to the public to disclose; or

(c) where the member's interests require disclosure (for example to enable the member to defend civil or criminal proceedings, or disciplinary proceedings); or

(d) where the disclosure is made with the express or implied consent of the client.

If a member believes that one of the exceptions (a) to (c) above may apply, it will usually be right to take independent legal advice, and he should inform his client accordingly.

See also paragraphs 8.13 to 8.16.

3.28 The phrase "an ordinarily competent inspector" (used in paragraph 3.24) is drawn from the Olin Energy case. The member should ensure that, on all points on which he has concluded that disclosure is required or is desirable, sufficient information is provided in the return, computation, supporting schedules or correspondence to enable such an inspector to appreciate what position is being taken by the taxpayer.

3.29 Normally, disclosure obligations are fulfilled by ensuring that relevant facts are reported in the statutory return form. In many cases, notably business accounts and computations, much of the information will be in a non-statutory form. Specific disclosure may not be needed if the information is already before the inspector dealing with the matter, for instance because the relevant facts have already been specifically stated in, or could clearly be deduced from, other information provided to the inspector in connection with the same tax affairs of the same taxpayer. In this respect the Revenue have stated that only information provided within the last three years should be considered as being available to the inspector. If a member is unsure whether the inspector will have the relevant facts or information available, he should draw the inspector's attention to them, for example by giving cross-references.

3.30 The Revenue have also stated that information provided to the Revenue's Head Office, or to another Revenue office, cannot be assumed to be before the inspector dealing with the matter. Similarly, information provided for a different purpose to the tax office dealing with the taxpayer's affairs, for example where the individual is a partner in a partnership and the same inspector also deals with the taxpayer's farm accounts, may need to be drawn to the inspector's attention.

3.31 A member should take reasonable steps to ensure that no information the disclosure of which is required by law is withheld from the tax authorities. Normally, there is no need to provide gratuitous information, information which the member understands to be in the possession of or available to the inspector in accordance with the remarks in paragraphs 3.29 and 3.30, information which has no bearing on tax, or information in excess of that requested by the Revenue or needed to secure agreement of computations or assessments. However, information which the member considers to be relevant should never be concealed from the Revenue, nor should facts and information be deliberately presented in such a way that a misleading impression is likely to be created. While obviously the taxpayer or member should not obscure any particular matter, there is no obligation specifically to draw attention to it, provided that the taxpayer (as advised by the member) is satisfied that the return is correct and complete and complies with the advice given in these guidelines.

3.32 A member is expected to exercise sound professional judgement and should not invite unnecessary, time-consuming enquiries from the Revenue, which may lead to unnecessary additional costs. However, if a taxpayer wishes to be reasonably certain of obtaining the protection of the *Cenlon* and *Olin Energy* decisions, it should be recognised that the Revenue are likely to contend that failure specifically to draw a particular point to the inspector's attention will deny the taxpayer any protection against a "discovery" in the future. Annex E provides the Revenue's views on the issue while observations of leading counsel on them are set out in Annex F.

3.33 Subject to the other points set out in these guidelines, members and their staff should recognise that the Revenue will expect them to bring their technical expertise to bear in relation to any schedules prepared by them and consider carefully information presented by them on behalf of their clients. See also the comments in paragraphs 3.43 to 3.48.

3.34 A member is entitled to assume that an inspector will be broadly familiar with but not an expert in:

(a) the normal terminology adopted by the accountancy profession in relation to financial accounts, as well as the books of prime record;

(b) generally-accepted accounting principles and financial reporting standards;

(c) the requirements of the Companies Acts so far as they relate to accounting matters;

(d) generally-accepted auditing principles; and

(e) the background to, and relevance of, the usual wording of audit reports

and will understand that the accounts of unincorporated and small corporate businesses may not have been audited.

3.35 The Revenue have established a number of internal administrative procedures (for example, of not examining every set of business tax computations every year). A taxpayer's reporting and disclosure obligations are not affected by such procedures. As they have no statutory force, they cannot of themselves create additional obligations on the part of the taxpayer.

3.36 Members in industry and commerce who are responsible for the preparation and submission of tax returns and computations should review the availability of information from companies for which they are responsible, to ensure that they have access to all the data which they consider they will require to enable them to fulfil their responsibilities.

Relevant responsibilities

3.37 The taxpayer has the primary responsibility to submit a correct and complete return or computation. Similarly, when additional information is provided, whether arising out of correspondence with the Revenue or otherwise, the taxpayer is ultimately responsible for ensuring that such information is correct and complete. In this context, the words "correct and complete" should be interpreted as meaning correct and complete to the best of the taxpayer's knowledge and belief, after making appropriate enquiries.

3.38 A member who prepares a return, computations, or supporting schedules on behalf of a client is acting as the client's agent and is responsible to the client for the proper presentation and disclosure of the facts.

3.39 A member is not required to audit the figures which appear in any financial statements additional to the statutory accounts (such as a detailed trading account) accompanying any return or business tax computations. Unaudited accounts submitted to the Revenue should be identified as such (for example, the UK branch accounts of an overseas company and partnership accounts).

3.40 Although, when preparing tax computations, a member is not required to re-audit or re-assess figures that appear in the accounts or other financial statements, the files of the member, or of the member's firm (including audit files) may contain information relevant for tax purposes, such as details of general provisions, or capital items included in revenue. Thus, where the member or the member's firm is also the statutory auditor or carries out a non-statutory audit to similar standards, the audit files should be reviewed to identify any adjustments for tax purposes. Similar considerations will apply to the accounts working papers where the member or the member's firm prepares the accounts of an unincorporated business.

3.41 A member who is responsible for preparing the tax return or computations but is not the auditor of the company or was not involved in the preparation of the accounts (for example, where tax computations are prepared by an in-house tax department or where an unincorporated business prepares its own accounts) should nevertheless take reasonable steps to be satisfied that appropriate adjustments are made when preparing the tax computations. This information may be obtained in a number of ways, including:

(a) arranging for the completion of a questionnaire or tax package designed, inter alia, to identify potential adjustments for tax purposes; or

(b) a review of any "link" papers, namely working papers showing the link between the accounting records and the statutory accounts or other financial statements.

3.42 Similarly, although a member is not required to "audit" information provided by the client, he should nevertheless bear in mind the need to exercise a critical function when acting as a conduit on behalf of a client. Normally, the member should review the overall credibility of the information provided to ensure that it appears reasonable based on the member's knowledge of the client's affairs, and to ensure that any relevant figures accord with relevant financial statements and associated tax computations. Similarly, a member should normally check that the information accords with other figures provided to the Revenue (for example, intra-group interest payments should correspond with the figures for receipts).

3.43 A member need not pursue speculative enquiries or attempt to check in detail information received unless there is a specific reason for believing that such additional work is necessary. As it is axiomatic that a client will be unwilling to pay for any work which a member carries out without the client's instructions, in the absence of any clear indication that further work is required a member is not obliged to question the accuracy of figures provided by the client, provided that he exercises a critical function.

3.44 It is the taxpayer (or in the case of a company an authorized person) who signs the return or is ultimately responsible for the submission of business tax computations. There is therefore a rebuttable presumption that all the information was provided by the client and that it has not been audited or independently verified by the taxpayer's agent, except to the extent required for other reasons (for example, the statutory audit of a company).

3.45 A copy of all tax computations should usually be sent to the client before submission to the Revenue. In exercising his professional judgement on this issue, a member should of course have regard to the instructions and wishes of the client.

3.46 A member should not appear to take responsibility for facts outside the member's knowledge. In such circumstances it is important that the inspector appreciates that the member is merely passing on information or statements provided by the client. Where this is not self-evident, members should put the matter beyond doubt by the use of wording such as :

(a) "we are informed [by our client] that ..."; or

(b) "the figures shown on Schedule xx were extracted from data provided to us by our client".

Where the accounts or information being presented to the inspector are not final, this should be clearly stated.

3.47 In no circumstances should a member pass on to the Revenue information that is known to be incorrect or misleading, whether in a letter written by the member or in a letter from the client which the member forwards to the Revenue. For further comments see Annex D.

3.48 Normally, a member should not have to "certify" facts or figures presented on behalf of the client. However, members should recognise that the Revenue may take account of the member's good name and reputation in considering the accuracy and reliability of information provided to them. A member's standing with the Revenue could be adversely affected if information submitted on behalf of a client is found to have been unreliable because of a member's failure to exercise due care in its submission.

Points on business accounts and related tax computations

3.49 Normally, the starting point for the computation of taxable profit is the profit shown in the financial statements of a business. In the absence of specific statute law or case law on the item in question, the figures shown in the financial statements are also valid in computing income or gains (and costs, expenses and losses) for tax purposes.

3.50 The financial statements referred to in paragraph 3.49 will have been drawn up having regard to the following principles:

(a) financial statements of a company have to show a "true and fair view", and satisfy company law requirements;

(b) generally-accepted accounting principles and financial reporting standards and the requirements of the Companies Acts have to be complied with;

(c) judgement will have been exercised in arriving at the appropriate and generally-accepted accounting treatment of a particular item, which may well vary for valid reasons (for example, variations in the items taken into account in valuing trading stock or work-in-progress); and

(d) where the financial statements are those of a company, responsibility for them lies with the directors. Auditors are required to give an opinion on those statements in accordance with generally-accepted Auditing Standards.

Further guidance on the responsibilities of auditors with regard to directors' reports and other financial information contained in an annual report of which audited financial statements form a part is set out in particular in Statement of Auditing Standards 160 (Other information in documents containing audited financial statements) in respect of audits of financial statements for periods ended on or after 23 December 1995.

3.51 Similar considerations apply to unincorporated businesses. In particular, experience shows that the Revenue expect to be provided with certain information regarding such businesses, including, where material, the extent to which cash differences, estimates and balancing figures have been used, and the reasons, where known, for any major deviations of gross profit percentages from the norm for that type of business.

3.52 Tax computations relating to a business, whether incorporated or unincorporated, are designed to supplement the information on the return form. They should therefore contain sufficient information to enable the inspector to settle the tax liability. Details known to be available to the inspector to the extent set out in paragraphs 3.29 and 3.30, including information contained in the financial statements submitted with the computations, need not be repeated. Each figure that appears in the accounts of a business should be adopted for tax purposes, provided that the ordinary principles of commercial accounting have been observed and that such adjustments as are required for tax purposes have been made. The concept of materiality is applicable in the preparation of the financial statements (for example, it may be the accounting policy in the business concerned to write off to revenue all amounts below a specified amount, including capital items) but is not normally applicable to adjustments in the tax computations. However, in particular cases it may be possible to agree certain tolerances with individual inspectors.

3.53 In relation to TMA 1970 s.99 (Assisting in preparation of incorrect return etc.), the changes then proposed by clause 161 of the Finance Bill 1989 were discussed at a meeting with the Revenue, the agreed notes of which were issued by the Institute of Chartered Accountants in England and Wales as TR759. These notes include the following:

> "187. The *ICAEW* considered that the provisions should be qualified to make it clear that auditors who correctly ignored small errors because they were not material did not fall within the ambit of s.99.
>
> 188. The *Revenue* explained that the revised wording corrected two lacunas in the wording of the present section, so that it applied generally to persons involved in the preparation of returns, accounts or other information to be used for tax purposes. These had come to light in the case of *Lord Advocate* v *Ruffle ([1979] SC 371)* and the amended wording was as recommended by Lord Jauncey in that case and endorsed by the Keith Committee. They added that, unlike other penalty provisions in the tax code where there were comparatively weak tests of culpability, s.99 applied only where a person had assisted in the preparation of a return or accounts which he *knew* to be incorrect. This requirement of *guilty knowledge* was the equivalent of *civil fraud* and required a correspondingly high level of proof. It followed that there could be no question of the situations which were of concern to the ICAEW - an auditor who noticed a small error but decided it was not material, or a person whose responsibility for an error was small - being caught by s.99."

Known Revenue practices

3.54 Particular care is needed if the Revenue have published their interpretation or have indicated their practice on a point and the client proposes to take a different view. Disclosure will probably be prudent in the interest of the client. Even where a taxpayer has counsel's opinion that the Revenue's interpretation is wrong, it is advisable to disclose the facts to the Revenue in writing making it clear that their interpretation is not accepted. However, the final decision on what, if any, disclosure is to be made rests with the client.

3.55 For this purpose, something should be regarded as an official Revenue position only if it is a written statement from the Revenue which is still current. Thus, it would include extra-statutory concessions, statements of practice, items included in "Tax Bulletin" and letters written to the member which give formal confirmation of general application on a technical point from the Head Office of the Revenue. On the other hand, the position taken by a particular inspector based on a particular set of facts should not be assumed to constitute a general and official Revenue interpretation.

3.56 In deciding what matters need to be disclosed, a member can rely on official Revenue practices (see paragraph 3.54) where these are favourable to his client. Care must however be taken to ensure that the facts of the particular case match those with which the extra-statutory concession or published statement of practice is dealing and that any further stated conditions or qualifications are fully met, for instance that the extra-statutory concession has not been used for the purpose of tax avoidance. As regards rulings on potential transactions or on those which have already taken place, as the decision in *MFK Underwriting Agencies Limited and others ([1989] STC 873)* makes clear, for the Revenue to be required to levy tax upon a basis inconsistent with the law because of some prior assurance as to the way that a particular transaction would be treated, it is ordinarily necessary for the taxpayer to be able to show that certain conditions are fulfilled. First it is necessary that the taxpayer should have placed all his cards face upwards on the table. This means giving full details of the specific transaction upon which a ruling is sought, indicating precisely what ruling is being asked for (and that it is a fully considered ruling) and the uses to which it will be put. Secondly, it is necessary that the ruling or statement relied on should be clear, unambiguous and devoid of relevant qualification.

3.57 The Revenue regard the Matrix Securities case as underlining the need for complete frankness in circumstances where taxpayers expect to rely on guidance given by the Revenue. Disclosure must be full, accurate, and fair as to the facts and the complete context in which the ruling is sought. An answer should not be sought in an unreasonable time, bearing in mind the complexity of the issues involved and the volume of material the Revenue has to examine. The Revenue consider it will invariably be appropriate in seeking guidance to spell out any uncertainties in the minds of members or clients on the specific points on which guidance is sought, and the legal issues involved, as well as making it clear for what purpose the ruling is required.

3.58 The text of a letter dated 3 June 1994 from the then Deputy Chairman of the Inland Revenue about requests for guidance following the decision in the Matrix Securities case is reproduced as Annex G. The Inland Revenue's Code of Practice 10 Information and Advice may also prove helpful.

4. DISCLOSURE UNDER SELF-ASSESSMENT

Introduction

4.1 With effect from 6 April 1996 the tax affairs of individuals, partnerships and trustees have been dealt with on a self-assessed basis. In the longer term it is intended to extend self-assessment to bodies corporate.

4.2 Self-assessment does not affect the responsibility of the taxpayer to report his income and gains truthfully and in a timely fashion. The general principles of Section 3 remain applicable under self-assessment. However, the "process now, check later" approach adopted by the Revenue means that the existing rules on disclosure have had to be adapted to provide the taxpayer with a measure of certainty.

4.3 Put simply, the Revenue are given until the end of the period ending twelve months from the normal filing date (later if the return is filed late) within which to raise enquiries into a return. If no enquiries are made during the period, the Revenue are debarred from reopening the return unless they are able to make a discovery which in turn is permitted only if there has been fraud or neglect on the part of the taxpayer or adequate disclosure was not made in the return.

Disclosure

4.4 Whether or not adequate disclosure has been made is determined by reference to the information available to the Revenue at a time when an enquiry could have been made into the return. In particular, information is available if:

(a) it is contained in the taxpayer's return, or a claim made by him, or in any accounts, statements or documents accompanying the return or claim; or

(b) it is contained in any documents, accounts or particulars provided to the Revenue in response to an enquiry or request; or

(c) it is information the relevance of which could reasonably be inferred by the Revenue from the above information or which is notified by the taxpayer in writing to the Revenue.

4.5 References to returns comprise the return for the year in question and the two preceding years.

4.6 On 31 May 1996 the Revenue published a press release on this subject, which is reproduced at Annex H.

Implications for members

4.7 The importance of achieving certainty in the context of self-assessment cannot be overstated. Under a Revenue-assessed system finality is achieved by agreement of an assessment. By contrast, under a self-assessment system there is no visible sign of finality if no enquiry is made into a return. It is therefore of fundamental importance that adequate disclosure is made by the taxpayer.

4.8 There is an important responsibility on members to ensure that their clients understand this, and to advise them on how to achieve finality. Accordingly, when preparing any tax return on behalf of a client, the member should consider whether any supplementary information ought to be sent to the Revenue, together with the return. He should ensure that the engagement letter and any relevant correspondence authorises the disclosure (see also "Practical Considerations", paragraphs 3.24 to 3.36 above).

4.9 Members should bear in mind that the mere submission of supplementary information does not necessarily meet the requirements of adequate disclosure. The member must also make sure that the relevance of the information can "reasonably be inferred" by the Revenue. How this can best be done will depend upon the circumstances of the case but some assistance may be gained from the views expressed by the Revenue in Annex H.

5. ACQUIRING KNOWLEDGE OF DIRECT TAX IRREGULARITIES

Generally

5.1 A member must do nothing to assist a client to commit any criminal offence, or to shield the client from the consequences of having defrauded the Crown of tax or of having been negligent in regard to direct tax matters. This is equally valid under both an assessed and a self-assessed system.

5.2 A member who suspects that an irregularity may have occurred should discuss the position with the client. This applies whether or not the member has acted in relation to the actual matter concerned. Members should be aware that Statement of Auditing Standards 110 (Fraud and Error) gives guidance to auditors which may have relevance in a fiscal context. Members are particularly referred to paragraphs 50 to 64 of that publication.

5.3 If there is doubt as to whether or not an irregularity has occurred the member should consider protecting his position by obtaining other advice (see paragraph 1.3).

Materiality

5.4 In considering the action which he should take in the circumstances outlined in this section, the member may take account of materiality but reference should be made to paragraphs 2.23 to 2.26.

Advice to be given where an irregularity is admitted

5.5 A member whose client has admitted an irregularity should advise the client in writing to disclose it to the Revenue. The member should explain the consequences of not doing so, in particular, that:

(a) should the Revenue discover the irregularity later there might be no defence against the imposition of penalties;

(b) having knowledge of the irregularity but suppressing it may be construed as a criminal offence or a civil fraud; and

(c) interest may accrue up to the time the tax is paid.

When the Revenue are not aware of an irregularity

5.6 Where there is an irregularity which the Revenue have not discovered, voluntary disclosure and payment of the tax will usually reduce the level of a penalty, although interest will remain due. The Revenue does not regard interest as penal, but merely commercial restitution for use of the money that was in fact due to the Exchequer. Prompt disclosure of an error may avoid suspicion by the Revenue that it was deliberate, thus reducing the risk of a civil fraud penalty.

When the Revenue allege that irregularities may have occurred

5.7 When the Revenue allege that an irregularity may have occurred, but it has not been identified by the member or his client, the member should assist his client by approaching the situation with care and objectivity.

5.8 The member should establish from the Revenue such details as he can of the alleged irregularity and the circumstances in which it occurred. This should take place at a meeting or in the course of correspondence, depending on the circumstances.

5.9 The member should then discuss the position with his client and establish with him the full facts relating to the alleged irregularity. The member should evaluate the Revenue allegations in the light of the facts as they have been found and where appropriate he should advise his client to make a full disclosure to the Revenue and to offer them all facilities for investigation.

5.10 It may be appropriate for the member, having agreed this with his client, to offer that a full report of the facts behind and surrounding the alleged irregularity be prepared by the member on behalf of the client with a view to making a full disclosure to the Revenue.

When the Revenue are aware of an irregularity

5.11 When the Revenue are aware that an irregularity has occurred, an interview under caution may be conducted. If the member is made aware of such an interview, he should notify his client of the seriousness of the proposed Revenue action and advise him to take advice from a criminal law specialist. It must be apparent to all that an interview under caution is an indication of the possibility of a criminal prosecution.

5.12 Interviews conducted by members of the Special Compliance Office are frequently carried out within the terms of Hansard practice as set out in Inland Revenue Code of Practice 9 (CoP 9, Special Compliance Office Investigations: cases of suspected serious fraud). The Hansard statement makes it clear that full disclosure and full co-operation are very important factors in their decision as to whether to seek a negotiated settlement. The Hansard statement also makes it clear that the Revenue always retain the discretion to prosecute in appropriate cases. A member should advise his client to make a full disclosure to the Revenue and ensure that at each meeting with the Revenue the client is represented by a professional adviser experienced in that type of investigation.

5.13 Until such time as it becomes apparent that criminal proceedings are being considered, for example the issue of a formal caution, a client should be advised to co-operate and make full disclosure in order to achieve maximum mitigation
of the penalty.

The importance of confirming admissions of irregularities by clients

5.14 A member should always ask for written confirmation of an irregularity by the client in as much detail as is available at that time. Reasons for this include the following:

(a) to minimize the room for doubt about the sum involved. In some cases the figure may be an estimate but it is important to clarify the extent of the admission; and

(b) to protect the member against any subsequent retraction by the client.

5.15 Misunderstandings can arise, especially when the client is under investigation by the Revenue. If a member were to inform the Revenue of an irregularity of a stated amount without having confirmed the amount with the client, the member could be in a vulnerable position if the client later claimed it was a lesser sum.

Instructions to disclose

5.16 If the client accepts the member's advice and instructs him to make a full and immediate disclosure, the member should write to the Revenue and either give full details or explain the position in general terms and say that the client has directed that a complete disclosure will be made as soon as possible. This letter should be provided to the Revenue as soon as possible in order to minimize the risk of their becoming aware of the problem before they are told. It would be improper to allow the Revenue to agree a settlement without putting them in possession of the full facts. The Revenue usually require a certificate of full disclosure to be signed by the client and it is vital that the client appreciates the importance of such a certificate.

Disclosure to other tax authorities of an admitted irregularity

5.17 The member should also consider the need to make a similar disclosure to other tax authorities

Unwillingness or refusal to disclose an admitted irregularity

5.18 "Unwillingness" in this context includes such procrastination or prevarication as effectively amounts to a "refusal", albeit not expressed. A member should allow a reasonable period for the client to make a decision. Thereafter the member must decide whether continuing "unwillingness" is in fact "refusal" for these purposes.

5.19 If the client refuses to accept the member's advice to make a full and prompt disclosure to the Revenue, the member should ensure that his conduct and advice is such as to prevent his own probity being called into question. It is essential therefore to advise the client in writing properly and fully of the consequences of the failure to disclose.

5.20 The member should explain to the client the Revenue's wide-ranging powers to obtain information from taxpayers and their agents. The client should be told that there is a considerably greater likelihood of a criminal prosecution (with the possibility of imprisonment) where the Revenue "discover" a fraud than where the client makes a voluntary disclosure and offers a suitable monetary settlement, and that voluntary disclosure normally results in a lower scale of penalty.

Where the member has acted in relation to the irregularity

5.21 A member who has acted in relation to the irregularity should make it plain that if the client refuses to authorise disclosure, the member must cease to act for the client in all matters, not just those related to direct tax save that the member is entitled to take the view that he is not obliged to cease to act where the amounts are not material. The member should also explain that if the client refuses to disclose, the member must act in accordance with paragraph 5.22. The client should be left in no doubt that this step could result in the Revenue commencing enquiries which might lead to the discovery of the non-disclosure and possible offence.

5.22 If, despite fully advising the client of the consequences the client still refuses to disclose to the Revenue, the member should forthwith:

(a) cease to act for the client in all matters and inform the client in writing accordingly;

(b) inform the Revenue that he has ceased to act for the client; and

(c) if the matters in question affect accounts or statements which carry a report signed by the member as to their accuracy, inform the Revenue that he has information indicating that the accounts or statements cannot be relied upon.

The passage suggested in paragraph 2.2 for inclusion in the engagement letter is particularly important in this connection. Members should bear in mind that they might otherwise be accused by the client of acting in breach of their professional duty.

5.23 The member should explain the practical hurdles to the appointment of a new adviser, if he ceases to act, in that it is the duty of professional advisers before accepting professional work to communicate with the person who previously acted in connection with that work.

5.24 Even where the member follows paragraph 5.22(c) he is under no legal duty to explain to the Revenue the reasons why the returns, accounts, etc. are defective, and should do so only with the former client's permission.

Where the member has not acted in relation to the irregularity but has acted in relation to other tax matters

5.25 The member may discover a material irregularity which occurred either before the engagement began or in relation to matters dealt with by another adviser or by the client himself, for example PAYE, NIC and returns on forms P11D. In such cases, the member should advise the client to make full disclosure to the Revenue. If the client refuses to disclose, the member should cease to act because the relationship of trust which must exist between a member and the client will have been impaired and, just as importantly, the member's relationship with the Revenue would be prejudiced.

5.26 However, as the member has not acted in those tax matters to which the irregularities relate, the member's duty is merely to inform the Revenue that he has ceased to act.

Where the member has not acted in relation to tax matters

5.27 A member who has not acted in relation to tax matters, but discovers or suspects that a client has committed a tax irregularity, should discuss the position with the client. If the client confirms the discovery or suspicion the member should ask the client to discuss the situation with the tax adviser with a view to making full disclosure to the Revenue. If the client refuses, paragraph 5.20 applies.

5.28 The member's duty is limited to encouraging disclosure to the Revenue. It is thereafter for the client to decide how to proceed. The member is not required to take the steps referred to in paragraphs 5.21 to 5.24. However, in the event that the client fails to make the disclosure, the member should consider whether the relationship with the client, which is based on trust, has been impaired and, if it has, whether it is proper to continue to act for the client. A member who decides to continue to act should not thereafter give any advice in relation to any tax matters (other than the matter of disclosure) unless and until the client agrees to disclosure to the Revenue.

When the client refuses to admit an irregularity

5.29 Where the client denies any wrongdoing to the satisfaction of the member, the member is free to continue to act for that client. The member should protect himself by ensuring that his files fully document the discussions with the client and the reasons why the member is satisfied with the explanations given.

5.30 Where the client denies any wrongdoing and the member rejects outright that denial, the member must cease to act for the client. The member should inform the Revenue that he is no longer acting on behalf of the client and should consider whether he should act in accordance with paragraphs 5.21 and 5.22.

5.31 Where, despit the client's denial of any wrongdoing, the member still has reservations, but does not consider that he is justified in rejecting the denial outright the member must give careful consideration as to whether he can continue to act on behalf of the client. Having exercised his judgement, the member should then proceed having regard to paragraphs 5.29 and 5.30.

Suspicious circumstances

5.32 A member who acts in relation to tax matters and has good grounds to suspect that a client has committed a material tax irregularity should discuss the position with the client to confirm or remove the suspicion. This applies whether or not the member has acted in relation to the actual matter concerned. If the suspicion is confirmed, the member would then have actual knowledge of the irregularity and the guidance contained in this statement applies.

5.33 If the member finds no confirmation but remains suspicious such that the relationship of trust which must exist between the member and the client may have been impaired, the member should consider whether he should continue to act. Paragraph 5.31 applies. If the member is then approached by a new adviser, the member should consider his position in the light of paragraph 5.36.

Request for information from a new adviser

5.34 On changes in a professional appointment the initiative to request information lies with the new adviser who should obtain the proposed client's authorization to communicate with the member. The member should not volunteer information to a new adviser in the absence of any such request.

5.35 When the member receives a request for information from a new adviser, he should:

(a) seek authorization from the former client to disclose all relevant information to the new adviser;

(b) on receipt of such authorization, disclose all the information needed and reasonably requested by the new adviser to enable him to decide whether to accept the work; and

(c) to the extent that he is authorized to do so, discuss freely with the new adviser all matters of which he should be aware.

5.36 If the former client refuses permission, the member cannot disclose information to the new adviser. However, the member can refer the new adviser to the existence of correspondence in which the member has previously explained the position to the former client. The new adviser will then ask the client for copies of that correspondence.

5.37 The new adviser will therefore become aware of the non-disclosure and possible offence. Since the previous adviser will have resigned on the grounds of the client's unwillingness or refusal to disclose, it should follow that if the client continues to be unwilling or refuses to disclose, or refuses permission for the previous adviser to communicate with the new adviser, the new adviser should decline to act. However, the new adviser is entitled to consider, after taking his own advice, whether or not he comes to the same conclusion.

6. INLAND REVENUE ERRORS

Note: The Revenue have explained that this section presents them with major difficulties and in particular they do not see how "special circumstances" as in paragraph 6.3 could exist. They ask that members should take all possible steps to ensure that their clients pay the correct amount of tax due in law, even where following an error by the Revenue insufficient tax is demanded.

General

6.1 Throughout this section references to Revenue errors are to the position which may arise from the raising of an inadequate assessment, an under collection of tax or interest or an over repayment of tax or interest, in circumstances where it is apparent to the member that a mistake has been made by the Revenue. The mistake may be one of law (but see paragraph 6.6), or may be a calculation error, or a clerical error; equally it may arise from a misunderstanding on the part of the Revenue of the facts as presented. Reference should also be made to the Revenue publication CoP1: Mistakes by the Inland Revenue.

6.2 In this section references are made to de minimis amounts of tax. The Revenue have said that they accept that a trivial amount need not, on de minimis grounds, be disclosed, but they have not at present given any guidance on this matter.

6.3 Where the member becomes aware that the Revenue, in full possession of the facts, have made an error in dealing with the affairs of a client, the member should seek the client's authority to advise the Revenue of the error. If the client refuses to give that authority, the member should consider whether there are any special circumstances which might render the refusal reasonable. If there are not then, unless the amount of tax or interest at stake is de minimis, he should consider whether he should continue to act, bearing in mind both the importance for trust to exist between the Revenue and the member, and the exposure of both the member and the client to possible criminal or civil penalties should the Revenue not be informed of the error.

6.4 If, however, a member is specifically asked by the Revenue to agree a figure, he must, subject to paragraph 6.6, agree what he believes to be the correct figure; this may be a figure negotiated in the course of discussions following full disclosure of the facts and circumstances. He is not at liberty to accept a figure he knows to be incorrect, nor does he need to seek his client's authority to disclose to the Revenue their errors.

6.5 It may be prudent for members to include in their letters of engagement authority to advise the Revenue of errors, so that reference to the client is not needed. Where no such authority has been obtained, the procedure in paragraph 6.8 should be followed.

6.6 Where the Revenue make an assessment based on an interpretation of law other than that favoured by the member, the member should review the position carefully. If the member is satisfied that the full facts have been supplied, that the Revenue position appears to have been arrived at in the light of a proper understanding of those facts, and that in all the circumstances the Revenue's interpretation is a tenable one, he is not obliged to notify the Revenue of the consequences of his favoured interpretation. It would, however, be wise for him to inform his client of the position in case a further assessment is raised at a later date.

6.7 Counsel has advised that, in all other cases of excessive repayment or inadequate demand, unless the tax at stake is de minimis, the member should take the client's instructions. The client should be asked to authorise the member to advise the Revenue of the error, and warned of the possible legal consequences if he is reluctant to give the authority sought; such consequences might additionally include interest and penalties.

6.8 Because the member may himself commit a criminal offence under the Theft Act 1968 (see paragraph 6.11) through his involvement in obtaining an excessive refund, he should seek his client's authority to inform the Revenue of the error. If this is not forthcoming he should consider taking independent legal advice with a view to:

(a) notifying the Revenue in any event, and notifying the client of his action; and

(b) ceasing to act for the client.

6.9 Counsel has advised that, if the Revenue fail to take action when an error by way of under assessment is clearly pointed out to them, a member has no further duty in the matter.

6.10 A member should ensure that a written record is kept of all advice given to clients in connection with Revenue errors, and of any reassessment of his relationship with his clients. The member should also consider taking independent legal advice where he has any doubts as to the proper course of conduct to be followed. Revenue errors may cause expense to members, and thereby to their clients. Members should bear in mind that in some circumstances clients may be able to claim compensation. (See CoP1: Mistakes by the Inland Revenue.)

Legal considerations

Offences under the Theft Act 1968

6.11 Theft Act offences might apply when a repayment results from the error. The most likely offence is that of theft contrary to the Theft Act 1968 s.1. Such an offence is committed when a person dishonestly retains, intending to keep or use, money which he knows does not belong to him. Dishonesty is the core of this offence. If the defendant were to raise the defence that he did not consider what he was doing to be dishonest, the prosecution would have to prove:

(a) that what was done was dishonest by the ordinary standards of reasonable and honest people; and

(b) that the defendant himself must have realised (or would have, had he stopped to think about the matter) that what he was doing was by those standards dishonest.

It is no defence that the defendant did not himself regard his conduct as dishonest.

6.12 If, before an excessive repayment is received by a client, a member knows that it has been, or is about to be, made and he was in any way concerned, however innocently, in obtaining it, for example by sending in the repayment claim, but does nothing to draw the Revenue's attention to the error, the member risks liability to prosecution. The offence charged would be obtaining property by deception or procuring the execution of a valuable security, namely the repayment warrant, by deception, contrary to the Theft Act 1968 s.15 or s.20.

The offence of cheat

6.13 Revenue prosecutions for the common law offence of cheat are not uncommon. This is an ancient offence which requires proof of an intent to defraud or to prejudice the Revenue. The Revenue need to prove dishonesty, the test of which is effectively the same as that set out above.

6.14 The offence of cheat is certainly applicable to the dishonest obtaining or retention of over-repayments of tax.

6.15 Counsel has advised that mere failure to advise the Revenue that they have demanded insufficient tax, particularly if the amount is significant, may in strict law be sufficient grounds for a successful prosecution. Members are therefore warned that their clients have no valid defence to a charge of cheating in cases where they refuse to authorise the member to disclose to the Revenue an error of fact which results in such an underpayment.

6.16 The reality of the risk of such a prosecution being instituted, of course, depends on the facts of each case.

Other matters

6.17 Counsel has also advised that there is no legal obligation on a taxpayer, or a member, to press the Revenue to issue an assessment, even if by reason of the delay the assessment goes out of time, provided that the full facts and information have been supplied.

7. SUPPLEMENTARY GUIDANCE ON INLAND REVENUE ERRORS UNDER SELF-ASSESSMENT

7.1 With effect from April 1996, the tax affairs of individuals, partnerships and trustees have been dealt with on a self-assessed basis. In the longer term it is intended to extend self-assessment to bodies corporate. The purpose of self-assessment is to enable the Revenue to accept tax returns without further correspondence and to operate procedures whereby the onus is on the taxpayer to pay the correct amount of tax at the correct time without intervention by the Revenue, but subject to review.

7.2 Self-assessment clarifies what a taxpayer must do to discharge his responsibility to pay the correct amount of tax due in law. It explicitly links the completion of a tax return with the creation of the legal charge to tax (the "self-assessment"). In addition there is a greater need to get the tax right first time. As a result there is a greater onus on members acting as agents to assist their clients in this regard.

7.3 Revenue errors may arise under self-assessment. Members will need to be alert to the following types of error:

(a) failure to issue a calculation of tax payable if a taxpayer has elected for the Revenue to do so;

(b) failure to raise an assessment or amended assessment to tax when the initiative to take action rests with the Revenue; and

(c) failure to demand or collect tax properly payable once a return is submitted and/or a self-assessment has been made including underpayment of tax and interest.

See also paragraph 6.1.

7.4 When advising clients of possible action in the light of Revenue errors, members should firstly consider whether the taxpayer has made a return which constitutes adequate disclosure (refer to Sections 3 and 4). Only in this context should the impact of Revenue errors be judged when the onus is on the taxpayer to self-assess.

7.5 It is reasonable for members to weigh the cost to the client of rectifying errors or mistakes against the amount of additional tax at stake. (See also paragraph 6.2.)

7.6 Members are advised to include the form of words suggested in paragraph 2.2 in their letters of engagement. This will ensure that members have their clients' agreement in principle to inform the Revenue when an error is identified.

8. INVESTIGATION OF TAX ACCOUNTANTS

General

8.1 This section sets out circumstances relating to the law as it presently stands, and does not take account of possible changes arising from the Ely Review of TMA 1970, s.20A.

Background

8.2 The Revenue have specialist units, part of whose brief is to monitor and investigate the standards of practising accountants and tax practitioners.

8.3 Generally the investigator will seek a meeting with the member. In the first instance it may be that the investigator only outlines to the member the reasons for seeking a meeting. There is no legal obligation on a member to acquiesce. In order to enable the member to consider whether to agree to the request, he should request full details of the matters giving rise to the investigator's concerns. If a meeting is held, it is likely that the investigator will ask to examine one or more sets of working papers relating to clients of the member either immediately or shortly after the meeting. There is no legal obligation on the member to comply at that stage.

8.4 On the evidence available before, during, or after a meeting with the member the investigator will consider whether:

(a) the member may have committed a criminal offence such as false accounting, or conspiring with a client to defraud the Revenue; or

(b) the member may have committed an offence within TMA 1970 s.99 (see paragraph 8.8); or

(c) the member's standards may be otherwise unsatisfactory in that he has been negligent or incompetent in preparing accounts and returns for submission to the Revenue.

8.5 Any approach to a member by an investigator should be regarded as a serious matter, as should any request for access to working papers. A member who receives such an approach should consider taking the advice of a suitably experienced specialist in tax investigations at an early stage. A member who believes at any stage that criminal proceedings may be taken against him and who is not entirely confident of the legal position should take legal advice, especially in view of the conflict between refusal to co-operate and his obligation of confidentiality.

8.6 The Revenue's legal powers to obtain information are considered at Annex I. It should be noted that TMA 1970 s.20A enables a Revenue investigator to obtain access to a member's working papers, and that its operation is clearly restricted to those circumstances where a "tax accountant" has been convicted of a tax offence by a UK court or had a penalty imposed under TMA 1970 s.99. The Revenue can also obtain access to working papers for *specific* clients under TMA 1970 s.20(3) subject to the over-ride in TMA 1970 s.20B(11), and a warrant for entry and seizure under TMA 1970 s.20C would in practice give access to the working papers of all clients.

8.7 A negotiated civil settlement resulting in no penalty actually being imposed on the member does not enable the Revenue to use s.20A.

8.8 Before the Revenue are able to impose a penalty on any person under s.99 they have to prove that the person:

(a) had assisted in or induced the preparation or delivery of any information, return, accounts or documents; and

(b) knew, at the time of the preparation or delivery, that the items would be, or would be likely to be, used for some purpose of tax, and knew that they were incorrect.

The Revenue have confirmed that auditors who correctly ignored small errors because they were not material would not fall within s.99: see paragraph 3.53.

8.9 Following the case of *Inland Revenue* v *Ruffle* (*[1979] SC 371)* it is clear that because s.99 is a penalty section a very high standard of proof is imposed on the Revenue.

8.10 The Revenue normally act against an individual practitioner, and not against a firm as a whole. It is questionable whether there is any power to proceed under TMA 1970 s.20A in respect of a firm's working papers where the individual penalised under s.99 no longer has the firm's papers in his power or possession (see s.20A(1)).

8.11 SP5/90 (accountants' working papers) explains how the Revenue in practice use the powers available to them (see also Annex I, paragraph 10).

8.12 Even without reliance on any legal powers, a Revenue official can simply request a member to give access to a wide range of working papers. Members should consider the matters referred to below before agreeing to do so.

Confidentiality and freedom to disclose

8.13 There should be no disclosure of confidential client information without the prior consent of the client unless there is a legal right or duty to disclose. There is generally freedom to disclose where it is:

(a) in the public interest; or

(b) in the member's own interest (where paragraph 8.15 applies,); or

(c) required by statute.

8.14 The first and last options will generally not apply in the circumstances of Revenue scrutiny of the member's standards, but the member will need to consider whether it is in his own interests to give general access.

8.15 A member may disclose to the proper authorities information concerning a client where it enables him:

(a) to defend a criminal charge or to remove suspicion; or

(b) to resist proceedings for a penalty in respect of a taxation offence (typically TMA 1970 s.99).

8.16 The member is entitled to disclose confidential information only if put on notice that he is suspected of a criminal offence or of committing an offence within, effectively, s.99. Beyond that, access should not be given to client working papers without the client's prior consent.

Further considerations

8.17 Members should bear in mind that:

(a) the papers to which access is given may contain prima facie evidence of criminal offences by the member or a client;

(b) the papers may contain prima facie evidence of an offence within TMA 1970 s.99, leading to an award of penalties under which the Revenue could legally seek access to the accountant's working papers for all clients;

(c) if the member gives access to client working papers without the prior knowledge and consent of the client, he may be liable for breach of at least an implied term of the contract between the member and the client;

(d) other factors may deter the member from disclosing client working papers, such as a possible restriction on access included in the terms of professional indemnity insurance contracts;

(e) if access on a voluntary basis is refused the Revenue may exercise any of the statutory powers referred to above. Alternatively tax districts may be advised that the investigator has misgivings as to the member's standards, and that clients' returns and accounts submitted by the member should be viewed in that light; and

(f) the imposition of a s.99 penalty, or an agreement to enter into a civil settlement with the Revenue, may prejudice the status of the member as a fit and proper person for audit and other regulatory purposes.

Advice in practice

8.18 As stated in paragraph 8.5, a member who believes at any stage that criminal proceedings may be taken against him should take legal advice.

8.19 In particular, where the Revenue have alleged that the member may have committed an offence within TMA 1970 s.99, and it is clear that formal proceedings under s.99 may be taken against him, the member should consider disclosure of working papers in the light of paragraphs 8.13 to 8.17.

8.20 It may be appropirate, after discussions with the investigator, to suggest the appointment of an independent practitioner to review and report on a sample of the member's working papers; this still represents disclosure of confidential information and paragraph 8.16 applies. It is, however, likely that the investigator will still wish to have direct access to a sample of the member's working papers.

8.21 An independent practitioner may be able to negotiate a settlement on behalf of the member. A member is not always the best advocate in his own cause.

8.22 Where it is alleged by the Revenue investigator that the member's standards are unsatisfactory, but in circumstances falling short of the possibility of criminal proceedings or a penalty being imposed under TMA 1970 s.99, then generally the member should not give access to client working papers without the prior knowledge and consent of the client. Any member contemplating giving access to a Revenue investigator where paragraph 8.15 above is not in point should consider the matters at 8.13 to 8.17. The possibility of appointing an independent practitioner to represent the member, as discussed at 8.20 , should be considered.

8.23 The member may wish to seek guidance from the Institute in any of the above circumstances.

III VALUE ADDED TAX

9. DISCLOSURE TO HM CUSTOMS AND EXCISE

Relevant responsibilities in preparing VAT returns

9.1 The client has the primary responsibility to submit a true and complete VAT return to Customs. It follows that the final decision as to whether to disclose is the client's. A member who prepares a return on behalf of a client is responsible to the client for the accuracy of the return based on the information provided.

9.2 Where a member is acting as a "tax representative" for an overseas principal the obligations and liabilities of the VAT legislation are imposed jointly and severally on the client and the member. A member who acts in this way as a tax representative should seek indemnity from the client against failure by the client to provide information required. The member should also make clear in writing his obligation to disclose any irregularity to Customs (see Section 10).

9.3 A member is not required to audit the figures in the books and records provided by the client but should exercise normal care and judgement in preparing the return, and should record detailed figures in working papers.

Disclosure of specific transactions to Customs

9.4 Normally, specific transactions need not be described to Customs. Nevertheless, a member may recommend to a client that a particular matter be disclosed in order to avoid uncertainty.

9.5 In such a case the full facts concerning it, including the reasons for doubt, should be disclosed to Customs. The client can then generally rely on any unequivocal ruling in writing received from them on the point.

9.6 If a transaction is found to have been treated incorrectly but it can be shown that full information about it was disclosed to Customs, the client will be able to claim the benefit of the concession concerning misdirection given in the Ministerial undertaking known as the "Sheldon Statement" and reproduced as VAT Extra-statutory concession A11. The undertaking says "If a Customs and Excise Officer, with the full facts before him, has given a clear and unequivocal ruling on VAT in writing or, knowing the full facts, has misled a registered person to his detriment, any assessment of VAT due will be based on the correct ruling from the date the error was brought to the registered person's attention".

9.7 The meaning of full disclosure was considered in *Matrix Securities Limited v IRC ([1994] STC 272,)* albeit in the context of direct tax. Customs have stated that the Sheldon Statement will not be honoured in cases where a local VAT office has been misled to obtain a specific ruling.

9.8 When disclosing transactions on which the member has advised, extra care may be needed to ensure that the full facts are disclosed. The advice given must not be allowed to affect the member's objectivity.

9.9 Customs consider that they are entitled to over-ride their general guidance by a specific ruling relating to the affairs of a particular taxpayer. Whether a specific ruling is applied retrospectively will depend on whether the general guidance could reasonably have been read as covering the particular case.

Known Customs practices

9.10 Particular care is needed if Customs have published their interpretation or have indicated their practice on a point and the client proposes to take a different view. Disclosure will probably be prudent in the interests of the client. Even where a taxpayer has counsel's opinion that Customs' interpretation is wrong, it is advisable to disclose the facts to the client's local VAT office in writing making it clear that Customs' interpretation is not accepted. However, the final decision on what, if any, disclosure is to be made rests with the client.

Requests for rulings from Customs

9.11 Once the member is satisfied that it is appropriate to apply for a ruling he should ensure that the client understands the issues and implications of the proposed course of action. This advice to the client should normally be confirmed in writing.

9.12 All rulings should be confirmed in writing. If necessary the client, or the member, should write to Customs confirming the facts and the ruling which is understood to have been given.

9.13 If a written ruling appears to the member to be incorrect, he should consider whether it is clear that full facts were disclosed (the amount of VAT involved may be a material fact) and whether it is clear from the wording of the ruling that the officer of Customs has understood the question.

Effect of rulings and official practice

9.14 Members are entitled to rely on official Customs' practices and rulings where these are favourable to their clients.

9.15 However, there are limits to the extent to which Customs are bound by undertakings and statements of policy which they have given or issued. Examples of restrictions on a taxpayer's entitlement to rely on Customs' rulings are:

(a) The VAT tribunals will have regard to the strict terms of the law in their decisions and may ignore any Customs' advice or extra-statutory concessions which the taxpayer may have relied on even if they have been published in an official Customs' notice or leaflet; and

(b) The tribunals cannot take account of the Sheldon statement.

9.16 If Customs refuse to stand by a ruling given, whether generally or specifically to the client, there may be a remedy in judicial review before the High Court. Application may also be made to the Adjudicator or to the Ombudsman.

9.17 If an error was obvious in the records available when the control officer visited, this should prevent any suggestion of fraudulent evasion or recklessly negligent conduct entailing a criminal penalty; nor should there be any question of an accusation of conduct involving dishonesty which could lead to a civil penalty. However, the concession on misdirection explained in 9.6 will not apply unless it can be shown that the officer saw the records in question and failed to point out the error. By its very nature, this is difficult to prove.

Demands by Customs for information

9.18 Customs' powers to demand information and their policy on access to working papers etc are outlined in Leaflet 700/47: Confidentiality in VAT matters (tax advisers) Statement of Practice. See Annexes J and K.

9.19 Enquiries from Customs are often unexpected and informal and usually arise from a visit to the client. The member should consider whether authorization to reveal the information requested is needed from the client. The nature of the enquiry may not be immediately apparent and the position may need reviewing as it progresses.

9.20 A member who is in doubt about the implications of a question should consider asking for it to be put in writing so that a response may be agreed with the client.

10. ACQUIRING KNOWLEDGE OF VAT IRREGULARITIES

Generally

10.1 A member must do nothing to assist a client to commit any criminal offence, or to shield the client from the consequences of having defrauded the Crown of tax or of having been negligent in regard to VAT matters.

10.2 A member who suspects that a VAT irregularity may have occurred should discuss the position with the client. This applies whether or not the member has acted in relation to the actual matter concerned.

10.3 If there is doubt as to whether or not an irregularity has occurred the member should consider protecting his position by obtaining other advice (see paragraph 1.3).

Materiality

10.4 In considering the action which he should take in the circumstances outlined in this Section, the member may take account of materiality but reference should be made to paragraphs 2.23 to 2.26.

Advice to be given where an irregularity is admitted

10.5 A member whose client has admitted an irregularity should advise the client in writing to disclose it to Customs. The member should explain the consequences of not doing so, in particular, that:

(a) should Customs discover the irregularity later there might be no defence against a misdeclaration penalty;

(b) having knowledge of the irregularity without acting upon it may be construed as a criminal offence or a civil fraud; and

(c) interest may accrue up to the time the VAT is paid: the policy of Customs not to assess interest in "no loss to the revenue" cases may not be relevant.

When Customs are not aware of an irregularity

10.6 Where there is an irregularity which Customs have not discovered, voluntary disclosure and payment of the under-declared or over-reclaimed tax will usually remove the risk of a penalty, although interest may remain due. Prompt disclosure of an error may avoid suspicion by Customs that it was deliberate, thus reducing the risk of a civil fraud penalty.

10.7 Correction of errors up to a certain amount can be made on the current VAT return as part of the entries for that period. If this is done, neither penalties nor interest are due. If the net value of the errors is greater than the specified level this procedure is not available. Form VAT 652 is provided for the purpose of making a voluntary disclosure separate from the VAT return although its use is not mandatory.

10.8 Customs have stated that disclosure of errors after a visit date has been arranged will be rejected where there is reason to believe that:

(a) the errors were disclosed only because of the visit; or

(b) disclosure made during or after a visit was prompted only by Customs' enquiries.

Other voluntary disclosures made after the visit date has been arranged may, however, be accepted by Customs.

When Customs allege that irregularities may have occurred

10.9 When Customs allege that an irregularity may have occurred, but it has not been identified by the member or his client the member should assist his client by approaching the situation with care and objectivity.

10.10 The member should establish from Customs the exact details of the alleged irregularity and the circumstances in which it occurred. This should take place at a meeting or in the course of correspondence, depending on the circumstances.

10.11 The member should then discuss the position with his client and establish with him the full facts relating to the alleged irregularity. The member should evaluate Customs' allegations in the light of the facts as they have been found and where appropriate he should advise his client to make a full disclosure to Customs' and to offer them all facilities for investigation.

10.12 It may be appropriate for the member, having agreed this with his client, to offer that a full report of the facts behind and surrounding the alleged irregularity be prepared by the member on behalf of the client with a view to making a full disclosure to Customs.

When Customs are aware of an irregularity

10.13 Customs must caution persons whom they have reasonable grounds to believe may have committed a criminal (as opposed to civil) offence. When, therefore, Customs are aware that a serious irregularity has occurred, an interview under caution may be sought. If the member is made aware of such an interview, he should attempt to ascertain Customs' reasons for the interview and then notify his client of the seriousness and the potential implications of the allegations. If the interview under caution is already taking place, and no legal advice has been sought, the member should reiterate the need to take legal advice which should already have been referred to by Customs at the outset.

10.14 The benefit of full co-operation and complete disclosure in civil fraud cases is set out in Customs Statement of Practice (VAT Notice 730). In criminal cases co-operation facilitates the negotiation of compounding of criminal offences (under s.152 CEMA 1979) and the mitigation of penalties.

10.15 An interview under caution is an early indication of the possibility of a criminal prosecution. If it appears likely that criminal charges will be brought, the member should advise the client to take advice from a criminal law specialist. Even if Customs are prepared to compound proceedings it may still be appropriate to take legal advice.

10.16 If the advice is to co-operate, the member should advise his client to make a full disclosure to Customs and when under investigation for civil evasion co-operate within the terms of VAT Notice 730. In the case of a criminal investigation under caution, full disclosure and production of documents etc should be undertaken throughout with the advice of a specialist professional.

10.17 Customs will advise the client at the outset if they are considering an investigation under the civil regime by issuing VAT Notice 730: this is not a caution. In the event of a criminal investigation a caution will be issued. Co-operation under the civil regime affords a maximum discounted penalty of 25% of the tax concerned: in the case of criminal investigations this should lead to a compounding (in all but the most serious cases) in lieu of criminal proceedings where co-operation can achieve mitigation of the penalty.

10.18 Members should be aware that Customs' current policy is not to offer the civil regime to professional advisers in respect of their own affairs.

The importance of confirming admissions of irregularities by clients

10.19 A member should always ask for written confirmation of an irregularity by the client in as much detail as is available at that time. Reasons for this include the following:

(a) to minimize the room for doubt about the sum involved. In some cases, such as undisclosed sales, the figure may be an estimate but it is important to clarify the extent of the admission; and

(b) to protect the member against any subsequent retraction by the client.

10.20 Misunderstandings can arise, especially when the client is under investigation by Customs. If a member were to inform Customs that a stated sum had been omitted from a return without having confirmed the amount with the client, the member could be in a vulnerable position if the client later claimed it was a lesser sum.

Instructions to disclose

10.21 Provided the member has the client's written confirmation (or a note of verbal instructions which he has confirmed in writing to the client) of an error too large to be corrected on the next return and instructions to disclose, he should write to Customs' giving as much detail of the inaccuracy in the return(s) as is available.

10.22 It may be considered more appropriate for the letter of disclosure to be sent by the client. In this case the member may draft the letter for the client and should in any case review it to ensure that adequate disclosure has been made.

10.23 This letter should be provided to Customs as soon as possible in order to minimize the risk of Customs' becoming aware of the problem before they are told. It would be improper to allow Customs' to agree a settlement without putting them in possession of all the facts.

Disclosure to other tax authorities of an admitted irregularity

10.24 The member should also consider the need to make a similar disclosure to other tax authorities.

Unwillingness or refusal to disclose an admitted irregularity

10.25 "Unwillingness" in this context includes such procrastination or prevarication as effectively amounts to a "refusal", albeit not expressed. The member should allow a reasonable period for the client to make a decision. Thereafter the member must decide whether continuing "unwillingness" is in fact "refusal" for these purposes.

10.26 If the client refuses to disclose an admitted irregularity the member should again write to the client making clear the consequences of a continued refusal.

10.27 If the client refuses to accept the member's advice to make a full and prompt disclosure to Customs, the member should ensure that his conduct and advice is such as to prevent his own probity being called into question. It is essential therefore to advise the client in writing properly and fully of the consequences of the failure to disclose.

10.28 If the client again refuses to disclose, the member should consider ceasing to act in relation to his VAT affairs, or all his affairs. The decision depends on the nature and scope of the member's relationship with the client having regard to the various circumstances. In considering what action to take where a client refuses to disclose to Customs a member may have regard to the materiality of the amounts involved. The member is entitled to take the view that he is not obliged to cease to act where the amounts are not material. Members are, however, referred to paragraphs 2.27 to 2.30 (Money laundering).

10.29 If Customs realised that the member had continued to act after becoming aware of such undisclosed errors, they might consider the member to be 'knowingly concerned' in the commission of an offence. At the very least Customs might cease to trust the member. Furthermore, the relationship of trust which must exist between member and client will have been impaired.

The member either prepares or assists in the preparation of the VAT return

10.30 Where the member either prepares or assists in the preparation of VAT returns, and the client refuses to disclose errors which occurred during the period in respect of which the member has acted, then subject to materiality, the member should cease to act in matters relating to VAT.

10.31 Where the error which the client refused to disclose occurred before the member started to act then the member should cease to act.

The member prepares or assists in the production of accounts

10.32 A member may prepare or assist in the production of accounts, without advising on VAT. If the client fails to disclose an irregularity, the member should consider whether the relationship with the client, which is based on trust, has been impaired and, if it has, whether it is proper to continue to act for the client. A member who decides to continue to act should not thereafter give any advice in relation to any tax matters (other than the matter of disclosure) unless and until the client agrees to full disclosure. This is again subject to materiality.

The member is engaged to provide VAT advice

10.33 If required to deal with Customs on the client's behalf, the member would not be in a position to do so in good faith whilst aware of an undisclosed irregularity and, subject to materiality, the member should cease to act. This does not apply where the member has advised on VAT matters, or otherwise, without dealing with Customs', but the member should consider his position carefully.

The member audits the accounts

10.34 Where the member is engaged solely to audit the accounts, failure by the audit client to disclose the irregularity despite advice to do so does not of itself place any obligation on the member to resign the appointment. Where other services are provided in addition, the member should proceed as indicated in the foregoing paragraphs.

Where the client refuses to admit an irregularity

10.35 Where the client denies any wrongdoing to the satisfaction of the member, the member is free to continue to act for that client. The member should protect himself by ensuring that his files fully document the discussions with the client and the reasons why the member is satisfied with the explanations given.

10.36 Where the client denies any wrongdoing and the member rejects outright that denial, the member must cease to act for the client in relation to his VAT affairs, or all his affairs. The decision depends on the nature and scope of the member's relationship with the client having regard to the various circumstances. In considering what action to take where a client refuses to disclose to Customs a member may have regard to the materiality of the amounts involved. The member is entitled to take the view that he is not obliged to cease to act where the amounts are not material.

10.37 Where the client denies any wrongdoing and the member still has reservations, but feels unable to reject the denial outright, the member must give careful consideration as to whether he can continue to act on behalf of the client. Having exercised his judgement, the member should then proceed in accordance with paragraphs 10.35 or 10.36, as appropriate.

Consequences of ceasing to act

10.38 The member need not inform Customs' of the cessation unless the member is at the time dealing with Customs' on the client's behalf.

Suspicious circumstances

10.39 A member who acts in relation to tax matters and has good grounds to suspect that a client has committed a material tax irregularity should discuss the position with the client to confirm or remove the suspicion. This applies whether or not the member has acted in relation to the actual matter concerned. If the suspicion is confirmed, the member would then have actual knowledge of the irregularity and the guidance contained in this statement applies.

10.40 If the member finds no confirmation but remains suspicious such that the relationship of trust which must exist between the member and the client may have been impaired, the member should consider whether he should continue to act. Paragraph 10.37 applies. If the member is then approached by a new adviser, the member should consider his position in the light of paragraph 10.42.

Request for information from a new adviser

10.41 On changes in a professional appointment the initiative to request information lies with the new adviser who should obtain the proposed client's authorization to communicate with the member. The member should not volunteer information to a new adviser in the absence of any such request.

10.42 When the member receives a request for information from a new adviser, he should:

(a) seek authorization from the former client to disclose all relevant information to the new adviser;

(b) on receipt of such authorization, disclose all the information needed and reasonably requested by the new adviser to enable him to decide whether to accept the work; and

(c) discuss freely with the new adviser all matters of which he should be aware.

10.43 If the former client refuses permission, the member cannot disclose information to the new adviser. However, the member can refer the latter to the correspondence in which the member has previously explained the position to the former client under the guidance in the previous paragraphs. The new adviser will then ask the client for copies of that correspondence.

10.44 The new adviser will therefore become aware of the non-disclosure and possible offence. Since the previous adviser will have resigned on the grounds of the client's unwillingness or refusal to disclose, it should follow that if the client continues to be unwilling or refuses to disclose, or refuses permission for the previous adviser to communicate with the new adviser, the new adviser should decline to act. However, the new adviser is entitled to consider, after taking his own advice, whether or not he comes to the same conclusion.

11. VAT AND ACCOUNTS

11.1 A member who prepares accounts should ensure that they reflect all material liabilities for VAT whether or not they have been declared to Customs. If a material liability for VAT is omitted an auditor cannot, without qualification, report on the accounts as showing a true and fair view. Customs' often request the accounts in the course of a control visit in an attempt to reconcile turnover to the VAT returns.

11.2 If an assessment based upon alleged undisclosed takings is accepted by the client or a settlement at a reduced figure is agreed with Customs, and the member has already submitted accounts information for the period in question to the Revenue, the member must consider whether the accounts are defective and if so follow the procedures in Section 5.

11.3 In such circumstances it may be wise to inform the Revenue before a final settlement is agreed with Customs in order that the self-assessment for direct tax purposes can be amended as well. This may help to avoid a second investigation.

ANNEX A
(para 3.6)

DISCLOSURE: SUMMARY OF RELEVANT INLAND REVENUE STATUTE LAW

General

A.1 The main provisions regarding returns of income and gains are set out in TMA 1970 Part II (ss. 7 to 12B); those relating to other returns and information are contained in TMA 1970 Part III (ss. 13 to 28). In each case, a specified person is required to provide the details set out in the relevant section. Returns must include a declaration that "... the return is to the best of his knowledge correct and complete". Under self-assessment, the Revenue have specific powers to enquire into returns. Such enquiries will cover the full range of return compliance activity by the Revenue, from questions related to a single entry ("aspect enquiries") to detailed investigations - ("full enquiries").

A.2 The reporting obligations fall into two categories:

(a) notice of liability to tax; and

(b) returns of income, profits and chargeable gains.

Notice of liability to tax

A.3 A person who is liable to tax is required to give notice of liability to tax where he has not delivered a return of profits, gains, or total income and has not received a notice requiring such a return, within a specified period after the end of a year of assessment (for an individual or trustee) or the end of an accounting period (for a company). The relevant sections are:

(a) notice of liability to income tax and capital gains tax (individuals and trustees) (TMA 1970 s.7;) and

(b) notice of liability to corporation tax (TMA 1970 s.10).

Returns

A.4 The obligations regarding returns for individuals are set out in TMA 1970 ss.8, 8A and 9. TMA 1970 s.8 requires an individual's personal return to contain "such information as may reasonably be required in pursuance of the notice" together with "such accounts, statements and documents, relating to information contained in the return, as may reasonably be so required" and new s.9 deals with the self-assessment of tax liabilities.

A.5 Partnership returns and the partnership statement now occupy new ss.12AA and 12AB. New s.12B deals with the record-keeping requirements under self-assessment.

A.6 Under corporate "pay and file", TMA 1970 s.11 in relation to corporation tax returns requires "such information as may be required ... together with such accounts, statements and reports as may be so required ... relevant to the application of the Corporation Tax Acts to the company". Normally the legislation does not explicitly require that any underlying calculations be shown in the return itself. Changes to s.11 and new s.11AA to cater for self-assessment of corporation tax are not expected to come into force until 1999 at the earliest.

ANNEX B
(para 3.8)

INLAND REVENUE TAX DEFAULTS: CIVIL ASPECTS (PRE SELF-ASSESSMENT)

General

B.1 This Annex deals with the civil (that is non-criminal) (aspects of tax defaults). Serious defaults, in particular those which involve or are alleged to involve some form of fraud, can have important implications under criminal law. Certain aspects of that topic are considered in Annex D.

B.2 The civil consequences of tax defaults arise under the TMA 1970 or subsequent statutes dealing with the same subject matter. There was a substantial recasting of the law in the FA 1989. It is helpful to remember that there are two classifications which have to be kept in mind:

(a) the different kinds of conduct which can constitute a default (see paragraphs B.3 and B.4 below); and

(b) the various consequences which can follow a default (see paragraphs B.5 to B.17 below).

The old law

B.3 Before the FA 1989, tax defaults fell within the three-fold classification of fraud, wilful default and neglect. "Fraud" and "wilful default" were not defined by statute. "Neglect" was defined by TMA 1970 s.118 (1) and (2).

The present law

B.4 The FA 1989 (principally by ss.149 and 159 and Schedule 17 Part VIII) made several changes to the old concepts. "Wilful default" and "neglect" disappeared altogether. There are now four kinds of default which are of major practical importance. They are fraudulent conduct, negligent conduct, failures, and errors. The changes in terminology and concepts may be more significant in form than in practical effect. In particular:

(i) anything which was wilful default under the old law will almost certainly be fraudulent or negligent conduct under the post-1989 law; and

(ii) anything which was neglect under the old law will very probably be negligent conduct under the post-1989 law.

Observations on each of the four kinds of default referred to in the post-1989 law are contained in the following sub-paragraphs.

(a) TMA 1970 s.36(1) as amended refers to "fraudulent ... conduct". TMA 1970 ss. 95 and 96 refer to a person who "fraudulently ... delivers" incorrect returns. There is no statutory definition of what is "fraudulent" in these contexts. The extensive case law about "fraud" under the pre-1989 law will presumably be relevant.

(b) The same sections of TMA 1970 (i.e. ss.36(1), 95 and 96) also refer to "negligent conduct", or to a person who "negligently delivers" incorrect returns. Negligent conduct presumably has many similarities to the old concept of "neglect", but whereas "neglect" had a statutory definition, negligent conduct does not. It is likely to have its common law meaning of a failure to observe the standard of care expected of a reasonable man in the circumstances concerned. The same will apply in the context of negligently delivering incorrect returns.

(c) "Failure" to give a notice, make a return, etc., required by or under the Taxes Acts can be relevant to the interest provisions of TMA 1970 s.88 (see paragraphs B.7 to B.10 below) and also to various sections concerning penalties (see paragraphs B.11 et seq. below). Before 1989 "failure" was expanded on for both purposes (s.88 interest and penalties) by TMA 1970 s.118(2) but, by reason of the insertion of a new s.88(7) in 1989, s.118(2) now applies only for the penalty provisions. In summary, the position now is as follows:

   (i) "failures" attracting penalties are regulated by s.118(2). For most practical purposes they are limited to failures without reasonable excuse to give the required notice, etc. The saving for cases where there is a reasonable excuse is the result of the second part of s.118(2). The first part of s.118(2) deals with slippage on statutory time limits: missing a time limit is not a "failure" for this purpose if the Revenue allow a longer time; and

   (ii) "failures" attracting section 88 interest are not regulated by s.118(2), but by s.88(7). Missing a time limit is a "failure" for this purpose, and there is no provision to say that it is not if the Revenue allow a longer time. Nor is there any saving for reasonable excuse.

(d) An "error" in any information, return, etc., delivered to the Revenue can be relevant under TMA 1970 s.88 (default interest - see paragraph B.7 et seq. below). There is no definition of "error", and there is no "reasonable excuse" exception either, so it seems that an error still counts as an error for this purpose even if the taxpayer had a reasonable excuse for it.

Consequences of defaults

B.5 Defaults may give rise to any one or more of three different kinds of consequences, namely:

(a) extended time limits for assessment;

(b) s.88 interest; and

(c) penalties.

Which kinds of default give rise to which of the above consequences depends on the detailed statutory provisions and is summarised in the remaining paragraphs of this annex.

Extended time limits for assessment

B.6 The FA 1989 significantly changed the law. The Revenue can make assessments for up to 20 years back in cases of either (i) fraudulent conduct or (ii) negligent conduct. No distinction is drawn between the two for this purpose. The following points should be noted:

(a) it is no defence for the taxpayer to establish that the fraudulent or negligent conduct was committed by the agent, not by the taxpayer. (Contrast penalties, as to which see paragraph B.16 below);

(b) the rules in the 1989 Act apply to assessments for all years from 1983-84 onwards. For earlier years the old rules still apply;

(c) under the old rules the Revenue could make assessments without time limit in cases of fraud or wilful default but had more limited powers in cases of neglect; and

(d) the major changes under the 1989 Act rules are that the Revenue's powers are cut down in cases of fraud (by the 20 years limitation), but conversely have been extended in most cases of what used to be neglect and is now negligent conduct.

Section 88 interest

B.7 In certain cases where a default leads to late payment of tax the taxpayer is liable to pay interest under TMA 1970 s.88 rather than s.86. Although the rates of interest are the same under the two sections, s.88 interest normally runs from an earlier date.

B.8 The kinds of default which attract s.88 interest depend on whether or not the conduct occurred before 27 July 1989 (the date of Royal Assent to the FA 1989).

(a) Before 27 July 1989 the relevant kinds of default were "the fraud, wilful default or neglect of any person". Accordingly all three of the old kinds of default attracted s.88 interest, and still do if they occurred before 27 July 1989. The words "of any person" indicate that the taxpayer would be liable for s.88 interest even if the default was that of his agent.

(b) On and after 27 July 1989 the kinds of default relevant for s.88 interest are:

(i) "failures" to give notices, make returns, etc.; and

(ii) "errors" in information, returns etc., delivered to the Revenue.

B.9 As to what are "failures" and "errors" see paragraph B4(c)(ii) and (d) above. It is worth observing that (since the introduction of a new s.88(7) in 1989) a failure or error for which the taxpayer had a reasonable excuse is still a failure or error for the purposes of s.88. Thus reliance, however reasonable, by a taxpayer on his agent cannot by itself protect him against s.88 interest if the failure or error arises in information or documents delivered on or after 27 July 1989.

B.10 Attention is drawn to SP6/89, articles in the Revenue Tax Bulletin issues numbers 4 and 7 and TAX 8/93 issued by the Institute of Chartered Accountants in England and Wales, in which the Revenue indicate their practice as to the circumstances in which they will consider charging s.88 interest where there is delay in submitting a tax return, or an error in the return.

Penalties

B.11 The most important penalties arise in three kinds of case:

(a) where a taxpayer does not notify chargeability (see paragraph B.12);

(b) where a return is not made or is made late (see paragraph B.13 below); and

(c) where a return is made but is incorrect (see paragraphs B.14 to B.17 below).

B.12 Persons who are chargeable to tax but do not receive return forms are obliged to notify chargeability within 12 months of the end of the year of assessment or (for companies) accounting period. If they do not and their omission is a "failure" (as to which see paragraph B.4(c)(i) above) they are at risk of penalties, the maximum being equal to the tax chargeable.

B.13 Penalties for not making returns or for making them late also rest on "failures", as to the meaning of which see paragraph B.4(c)(i) above. The FA 1989 (for pay and file F(No 2)A 1987) increased the amount of the penalties, especially for failures which continue for more than a year. For details see TMA 1970 ss.93 and 94. There are also penalties for "failure" to comply with any of an extensive list of specific requirements listed in TMA 1970 s.98.

B.14 Penalties for incorrect returns may be exacted in cases of fraud or negligence. For returns delivered on or after 27 July 1989 the maximum penalty, for fraud as well as negligence, is equal to the tax on the amount by which the return is incorrect. This is a relaxation of the previous law in cases of fraud: for fraudulent returns delivered before 27 July 1989 the maximum penalty was £50 plus twice the tax.

B.15 There is no penalty for an "innocent" incorrect return, that is a return which is wrong but where the taxpayer was guilty neither of fraud nor of negligence. This is, however, subject to TMA 1970 s.97, whereby a taxpayer may be at risk of penalties if he fails to correct an error which subsequently comes to his notice. It is the Institute's understanding, supported by the opinion of leading counsel, that if a taxpayer in good faith receives advice from a person or firm whom he reasonably believes has appropriate and relevant experience and knowledge, and who has been given full particulars of the relevant facts, that a particular item need not be disclosed (for example, because it is not taxable) or that a particular expense is properly deductible, he is not negligent if he submits a return relying on that advice.

B.16 The Institute is advised that the position as stated in paragraph B.15 above remains correct even if the adviser on whom the taxpayer reasonably relied was himself negligent or even fraudulent. In cases of incorrect returns penalties are payable by the taxpayer only if the fraud or negligence is the taxpayer's own. TMA 1970 ss.95 and 96 are so worded that an innocent taxpayer cannot be required to pay a penalty for the fraud or negligence of an agent. The Revenue do not accept this view, but leading counsel's advice to the Institute is unequivocal.

B.17 However, in such a case the agent may himself be liable to a penalty under TMA 1970 s.99. The section applies where a person "assists in or induces the preparation or delivery of any information, return, accounts or other document which (a) he knows will be, or is or are likely to be, used for any purpose of tax, and (b) he knows to be incorrect". The maximum penalty is £3,000. A further consequence of a penalty under the section being imposed is that the Revenue obtain an extensive power under TMA 1970 s.20A to call for papers from the agent relating to the affairs of any of his clients (not just the client in respect of whom the offence was committed).

ANNEX C
(para 3.8)

INLAND REVENUE TAX DEFAULTS: CIVIL ASPECTS (SELF-ASSESSMENT)

General

C.1. This Annex deals with the civil (that is non-criminal) aspects of tax defaults. Serious defaults, in particular those which involve or are alleged to involve some form of fraud, can have important implications under criminal law. Certain aspects of that topic are considered in Annex D.

C.2. The civil consequences of tax defaults arise under the TMA 1970 or subsequent statutes dealing with the same subject matter. There has been a substantial recasting of the law in the Finance Acts 1994 and 1995 to cover the self-assessment regime.

Outline of the self-assessment regime

C.3. The FA 1994 contained the main legislation for the major reform of the tax system by the introduction of self-assessment. This was built upon in the FA 1995. For most taxpayers these changes have effect from 1996/97.

C.4. The key change is that taxpayers create the legal charge to tax by making a "self-assessment" of their tax liability for any year. These self-assessments replace the Revenue assessments issued under the old system. There are certain limited occasions when an assessment will continue to be issued under the new regime.

C.5. Self-assessment introduces a requirement to file returns by a fixed date and to pay all income tax (from whatever source) and capital gains tax by fixed dates. Two payments on account maybe required, based on the previous year's income tax liability. Then a balancing payment, comprising the balance of the income tax due and any capital gains tax, is payable by 31 January following the year of assessment. There are automatic sanctions for failure to comply with these dates.

C.6. The Revenue will initially process the return (and payment) as submitted by the taxpayer subject to a statutory right to correct obvious errors. Only a limited number of formal enquiries will be made. Any such enquiry must be started within fixed time limits. This is known as the "process now - check later" system. It represents a completely new approach to the critical examination of returns and once the initial process is complete the Revenue have an explicit right to enquire into the completion and accuracy of any return, supported by new information powers.

C.7. Random selection plays an important part in the new regime but, as hitherto, the vast majority of enquiries will be selected on the basis that tax is thought to be at risk. Taxpayers have a right of appeal if they do not agree with the Revenue's findings, and have the right to ask the Commissioners to issue a completion notice to bring the enquiry to an end. The Revenue also retain general investigative powers. (See also paragraph C.21 below.)

C.8. The self-assessment partnership return includes a partnership statement summarising the profits and losses made by the partnership in the return period, and the shares of those profits and losses allocated to each partner. This return has its own filing dates and compliance regime quite separate from that applying to the partners' personal returns. The partners have collective responsibility for the partnership return, through a partner nominated to act on their behalf. But there is no longer joint responsibility for the tax due on partnership profits. Instead, each partner is required to include his share of partnership profit (or loss) in his own self-assessment, and to pay tax accordingly.

C.9. Self-assessment will apply to corporation tax returns for accounting periods ending on or after 'the appointed day' which will not be before early 1999. Self-assessment therefore will not apply to most companies until 1998 at the earliest.

The new interest regime

C.10 Interest is chargeable under TMA 1970 s.86 on any amount of tax unpaid at the due date for payment, whether payment on account or balancing payment. Where an amendment to a self-assessment or a discovery assessment is made after the filing date, interest will run from the annual filing date for the relevant tax year. Interest applies to all late payments of tax, surcharges or penalties.

Surcharges

C.11 In addition to interest, surcharges under TMA 1970 s.59C apply at 5% of tax still outstanding more than 28 days after the due date and a further 5% if tax is still outstanding six months later. (This does not apply to payments on account.) Unpaid surcharge attracts interest 30 days after it has been imposed.

C.12 An appeal against a surcharge may be made to the Commissioners on the grounds that the taxpayer had a reasonable excuse (other than the inability to pay) for the late payment. The Board has the power to mitigate surcharges.

Penalties

General

C.13 The Revenue have the power to mitigate penalties (TMA 1970 s.102). An appeal to the Commissioners can be made against any penalty determination made by the Revenue (TMA 1970 s.100B). For most penalties, the Commissioners can confirm, increase, decrease or set aside the determination.

Late filing

C.14 Automatic fixed penalties apply if the time limits for the filing of tax returns are not met. The initial penalty is £100 (TMA 1970 s.93(2)) and if the return remains outstanding six months after the filing date there is a further penalty of £100 unless an officer of the Board has already applied to the Commissioners for a daily penalty (TMA 1970 ss.93(3) and 4(4)). Fixed penalties apply to all cases of late filing but they cannot exceed the tax liability for the year (TMA 1970 s.93(7)).

C.15 An appeal against a fixed penalty may be made to the Commissioners but their power is restricted to confirming or, if the taxpayer has a reasonable excuse for the failure, setting aside a determination only (TMA 1970 s.93(8)).

C.16 In addition to fixed penalties a daily penalty of up to £60 per day may be imposed if leave is given by the Commissioners (TMA 1970 s.93(3),(6)).

C.17 If the failure to file the return continues for more than twelve months after the filing date an officer of the Board may impose a tax-geared penalty. This cannot exceed the tax liability for the year (TMA 1970 s.93(5)).

Incorrect returns

C.18 The existing rules for penalties following the fraudulent or negligent filing of an incorrect return continue to apply in respect of all self-assessment returns (TMA 1970 s.95). The maximum penalty is 100% of the tax not paid as a result of the incorrect return.

C.19 Under TMA 1970 s.36 an assessment for the purpose of making good to the Crown a loss of tax attributable to fraudulent or negligent conduct may be made at any time not later than twenty years after the 31 January next following the year of assessment to which it relates. Where the fraudulent or negligent assessment relates to a partnership return extended time limit assessments may be made on the partners.

Enquiries into returns

C.20 The Revenue may enquire into a return and failure to comply with a notice for this purpose under TMA s.19A requesting documents, accounts or other particulars can result in a penalty (TMA 1970 s.97AA). The initial penalty is £50 but if failure continues after the determination of the penalty additional daily penalties may be imposed. If these are determined by an officer of the Board the maximum penalty is £30 per day; if set by the Commissioners in formal proceedings the penalty rises to a maximum of £150 per day (TMA 1970 s.97AA(2),(3)).

Record keeping

C.21 It is emphasized that the new procedures under TMA 1970 s.19A(1),(2) apply only where formal notice of enquiry into the return has been issued and are part of the "process now - check later" regime. They apply only where the accuracy of the return is being checked within a fixed timescale in which enquiry can be started. The general investigative powers which can be used in a wide variety of circumstances continue to apply. They fulfil two separate and distinct functions:

(a) under TMA 1970 s.20 which allows information to be sought relating to any tax liability to which the taxpayer may or may not be subject. They are not restricted to a particular return or period and can be used to obtain information from third parties;and

(b) the ability to obtain a Commissioners' precept under SI 1994/1811 (Special Commissioners) and SI 1994/1812 (General Commissioners) has been preserved.

C.22 TMA 1970 s.12B imposes a requirement to keep records. There is a penalty of up to £3,000 for each failure to keep or preserve adequate records (TMA 1970 s.12B (5)).

Claims and elections

C.23 Wherever possible claims and elections should be included in the self-assessment return. TMA 1970 s.42 and Schedule 1A cover claims and elections not made in the return.

C.24 The return as a whole remains subject to the "check later" regime. The Revenue have an automatic right to enquire into claims which form part of the return or are made separately (TMA 1970 s.9A and Schedule 1A, para 5). A penalty of up to £3,000 may be charged for each failure to keep or preserve adequate records in support of a claim (TMA 1970 Schedule 1A, para 2A(4)).

Notification of liability

C.25 Under TMA 1970 s.7 taxpayers who do not receive a tax return are still required to notify chargeability to income tax or capital gains tax within six months from the end of the tax year in which tax liability arises. This does not apply if there were no gains, no liability to tax or sufficient tax deducted at source to cover the liability. The penalty for non-compliance is tax-geared.

Agents

C.26 Any person who assists in or induces the preparation or delivery of any information, returns, accounts or other document which he knows will be used for tax purposes and which he knows to be incorrect will be liable to a penalty not exceeding £3,000 (TMA 1970 s.99). The extensive powers to call for the tax accountant's papers in such circumstances remain (TMA 1970 s.20A).

Discovery

C.27 The vast majority of assessments issued by the Revenue under self-assessment will be discovery assessments under TMA 1970 s.29 which has been recast to provide general rules for Revenue assessments to prevent any loss of tax, but new rules limit the right to make a discovery assessment for any period if a self-assessment has already been made by the taxpayer for that period.

C.28 Discovery assessments will be limited to those where the taxpayer has been fraudulent or negligent or has failed to disclose all relevant information.

C.29 There can be no discovery assessment if the self-assessment return was made on the basis of a view of the law prevailing at the time despite the fact that opinions may have subsequently changed (TMA 1970 s.29(2)).

Revenue determinations where no return delivered

C.30. Under TMA 1970 s.28C where a self-assessment return is not filed on or before the appropriate filing date an officer of the Board may make a determination of the tax due. This determination is served on the taxpayer and treated as a self-assessment until such time as the self-assessment is filed. There is no right of appeal, but the determination is automatically displaced by the taxpayer's own self-assessment once made.

Partnerships

C.31 TMA 1970 s.93A deals with failure to make a partnership return. There are fixed and daily penalties for failing to file a partnership return. If time limits are not met fixed penalties automatically arise and in more substantial cases additional daily penalties may be sought. The initial penalty is £100 for each partner who was a member of the partnership during the period covered by the return and will be charged on individual partners, not the partnership. If the return is still outstanding six months after the filing date a further penalty of £100 per partner will be due unless daily penalties are already being sought.

C.32 There is no provision for these fixed penalties to be restricted where the tax due on the partnership profits is minimal. A composite appeal against the fixed penalties may be made by the representative partner on behalf of all the partners. The penalties can be set aside only if there is reasonable excuse for the whole period of delay.

C.33 In addition to fixed penalties a daily penalty of up to £60 per relevant partner per day may be applied if leave is given by the Commissioners. A composite appeal on behalf of all the partners may be made against daily penalties by the representative partner.

C.34 Penalties are charged on individual partners, not the partnership.

C.35 Where a partner fails to file a personal return on time and the partnership return is also late that partner will be liable to two sets of fixed penalties. But there is no tax-geared penalty in respect of the late partnership return because the partnership is no longer liable for any of the tax on partnership profits. Where an individual partner's return is late the tax on the partner's share of the partnership income will be included in the calculation of the tax-geared penalty chargeable on the partner.

C.36 Self-assessment enquiry procedures will apply to partnership statements under TMA 1970 s.12AC. A notice of enquiry into a partnership statement will be treated as including a notice of enquiry to each of the members of that partnership who have filed their own personal returns. This does not mean that non-partnership aspects of a partner's return are automatically under enquiry. These can be reviewed only if a separate enquiry is opened under TMA 1970 s.9A or, if the time limit has passed, if the discovery rules apply. Similarly the completion of an enquiry into one part of the return (for example partnership income) has no consequence for any separate enquiry into, say, non-partnership income. An enquiry into an individual partner's return does not automatically open up the partnership statement for enquiry (TMA 1970 s.12AC(3)).

C.37 The Revenue have the same rights to call for partnership documents for enquiry purposes under TMA 1970 s.19A as it has for individuals, and the same penalties under TMA 1970 s.97AA apply for failure to file documents required.

C.38 Discovery assessments must be made on the individual partners but there are specific rules under TMA 1970 s.30B in respect of the partnership statement itself.

C.39 Where a representative partner submits an incorrect partnership return or incorrect accounts connected with that return or an incorrect statement or declaration connected with that return and does so fraudulently or negligently or as a result of fraudulent or negligent conduct by any other member of the partnership during the period covered by the return, each member of the partnership will be liable to a tax-geared penalty. Any such penalty will be computed on an individual basis by reference to additional tax that each individual partner is required to pay as a result of that offence (TMA 1970 s.95A).

ANNEX D
(para 3.8)

INLAND REVENUE TAX DEFAULTS : CERTAIN CRIMINAL ASPECTS

D.1 This annex deals with certain criminal aspects of tax defaults. The civil aspects are considered in Annexes B and C.

D.2 There is a wide range of criminal offences which can be committed by the taxpayer. Those offences include offences contrary to statute and common law.

D.3 The most common statutory offences charged are under the Theft Act 1968 and include:

(a) theft, contrary to s.1 (for example, in dishonestly retaining what are known to be overpayments of tax by the Revenue);

(b) obtaining property by deception, contrary to s.15, or procuring the execution of a valuable security by deception, contrary to s.20 (for example, dishonestly obtaining from the Revenue a refund of tax to which the taxpayer or member knows there is no entitlement); and

(c) false accounting, contrary to s.17 (for example, submitting or concurring in the submitting of false returns, or falsifying or concurring in the falsifying of false books of account).

D.4 Offences of forgery are also charged under the Forgery and Counterfeiting Act 1981.

D.5 It is also a criminal offence to incite a client to commit an offence whether or not it is in fact committed, or to help or encourage a client in the planning or execution of a criminal offence. If two or more people agree to commit a criminal offence, they can be charged with conspiracy to commit that offence.

D.6 A common law criminal offence that is often charged is cheating the Revenue. This covers matters as diverse as:

(a) the submission to the Revenue of what are known to be false accounts. It is irrelevant from the member's standpoint who actually signed or submitted the accounts, provided he himself:

(i) was party to their submission or their preparation;

(ii) knew that they were false; and

(iii) knew that they were to be submitted to the Revenue;

(b) the telling of a deliberate or material untruth (whether orally or in writing) to the Revenue;

(c) the submission to the Revenue by a member of a letter from the client containing what the member knows or believes to be a material untruth; and

(d) the dishonest failure to make a return to the Revenue.

ANNEX E
(paras 3.23
and 3.32)

INLAND REVENUE'S VIEWS ON "DISCOVERY ASSESSMENTS" STATEMENT OF PRACTICE SP8/91, 26 JULY 1991

General

E.1 This Statement of Practice explains, in relation to income tax, corporation tax and capital gains tax, the circumstances in which the Revenue seeks to recover tax when a person has not been assessed or has been inadequately assessed. The Statement does *not* cover cases where there may have been fraud or negligence by or on behalf of the taxpayer.

E.2 The Statement draws attention to the relevant statute and case law, in particular to the cases of

Cenlon Finance Co Ltd v Ellwood(1)and
Scorer v Olin Energy Systems Ltd(2)

E.3 The following paragraphs should be read as subject to the general proviso that it is fundamental to the operation of the tax system that it is for the taxpayer, who is in possession of the facts, to supply them to the Revenue so that his tax liability may be determined. Case law confirms that, if the relevant facts have not been accurately, fully and clearly disclosed by the taxpayer at the time, the Revenue should not regard agreements reached, or action taken or omitted by its officials as binding it to accept less than the full amount of tax legally due.

Inspectors' Discovery Powers

E.4 Section 29(3) of the Taxes Management Act 1970 provides that where, after an assessment has been made or a decision has been taken that an assessment is not required, an Inspector of Taxes discovers that any taxable profits have not been assessed, he may make an assessment in the amount he considers ought to be charged. Similarly, a further assessment may be made if an Inspector discovers that an assessment is insufficient or that a relief should be withdrawn. These powers may also be exercised by the Board. There are also other discovery provisions in the Taxes Acts which empower an Inspector to make assessments to recover excessive reliefs, tax unpaid and over-repayments of tax, for example Section 30 of the Taxes Management Act and Sections 252 and 412(3) of the Income and Corporation Taxes Act 1988. Normally any assessment or further assessment must be made not later than six years after the end of the chargeable period to which it relates (Section 34(1) of the Taxes Management Act).

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(1) [1962] AC 782; [1962] 2 WLR 871; [1962] 1 All ER 854; 40 TC 176

(2) [1985] AC 645; [1985] 2 WLR 668; [1985] 2 All ER 375; [1985] STC 218; 58 TC 592

E.5 The Courts have established that, subject to the decisions in the *Cenlon* and *Olin* cases, a change of opinion can amount to "discovery"; that discovery can be made by an Inspector other than the one who made the first assessment; and that discovery can extend to a finding that the law has been incorrectly applied as well as the coming to light of additional facts. The word has been held to include any situation in which for any reason it newly appears to an Inspector that a taxpayer has been undercharged.

The main principles

E.6 Two main principles are relevant in considering whether a discovery assessment may be made in any particular circumstances.

First, the Revenue does not go back on a specific agreement made by an Inspector on a particular point and raise a discovery assessment in respect of that point, whether or not the Inspector correctly took account of current law and practice in entering into that agreement;

Second, in circumstances where it cannot be said that the particular point was the subject of a specific agreement, the Revenue regards itself as bound by the Inspector's acceptance of a computation if the view of the point implicit in the computation was a tenable one.

But the Revenue does not regard itself as bound by any agreement made, or considered to be made, or any decision taken by an Inspector, if any of the information supplied on which that agreement or decision was founded was misleading.

The position in more detail

(i) Specific agreement: appeal cases

Cenlon

E.7 First, there is the case where there has been a specific agreement made by an Inspector on a particular point, ie where an issue has been raised expressly by the Inspector, the taxpayer or his agent (whether orally or in writing) and agreement has been reached on the treatment of that issue for tax purposes. The decision in the *Cenlon* case established that, if an assessment has been determined on appeal in accordance with Section 54 of the Taxes Management Act 1970, a discovery assessment should not be made in respect of any particular point which had been specifically dealt with in the course of the determination of that appeal.

Olin

E.8 The decision in the *Olin* case gives guidance on deciding whether (in the absence of express words making the position clear) a particular point has been agreed, or could be said to have been agreed, in the course of reaching an overall agreement on a person's tax liability for a particular period. The *Olin* case makes it clear that a particular point agreed may not only be an issue raised expressly by the Inspector, the taxpayer, or his agent, (whether orally or in writing), but also any point which was fundamental to the whole basis of the computation of the taxpayer's liability, and so clearly and fully described in the accounts or computations that its significance for the computation of the taxpayer's liability was clearly and immediately apparent. In these circumstances the Inspector could not reasonably be regarded as having agreed the computation without having appreciated and accepted the point. In other words the Inspector must have been clearly put on notice of the point.

E.9 The question whether a particular point is fundamental to the whole basis of the computation of the liability is one which must depend for its answer on the facts and circumstances of the particular case. At one extreme, there will be cases like *Olin* itself where the claim to set off the losses of the defunct trade against the profits of the continuing trade was fundamental in that it had a major impact on the computation of the liability and, moreover, was so clearly and fully described in the computations that the Inspector must have appreciated what was being claimed. In the House of Lords, Lord Keith concluded that the Inspector's agreement to the computations would have led a reasonable man to believe that the Inspector had decided to admit the claim. In circumstances like these, the Revenue would accept that the particular point was covered by the agreement reached and could not subsequently be the subject of a discovery assessment.

E.10 At the other extreme, there will be cases in which a point is not fundamental to the basis of the computation, in that it does not have a major impact on the liability, or it is not so clearly and fully described in the accounts or computations that its significance is clearly and immediately apparent from the information supplied. For example, in cases where the taxpayer or his agent are claiming a particular deduction in arriving at profits, and among a multiplicity of items contained in the accounts and supporting material is a piece of information which, if the Inspector had studied it in detail and thought through the implications, could have alerted him to the fact that the claim was not valid, the Revenue would not accept that a discovery assessment could not be raised in respect of the particular (incorrect) deduction. Moreover, if further information were needed before the Inspector could reasonably be expected to appreciate the significance of the point for the taxpayer's liability, the Revenue would not accept that the Inspector should be regarded as having considered and agreed that point.

E.11 The treatment of cases in between these two extremes must be a matter of judgement, depending on the particular facts. It will be necessary to decide, taking a reasonable and commonsense view of the matter, whether a taxpayer or his adviser would consider that a competent Inspector, in examining the accounts and computations, must be considered to have addressed his mind to the point at issue before signifying his agreement to the computation of the liability. This will be so only if the point was both fundamental to the whole basis of the computation, and was so clearly and fully described that its significance for the computation of the taxpayer's liability was clearly and immediately apparent. In these circumstances the Inspector could not reasonably be regarded as having agreed the computation without having appreciated and accepted the point.

(ii) Specific agreement: non-appeal cases

E.12 The principles established in the *Cenlon* and *Olin* cases strictly apply only where there was an appeal against an assessment or an appeal against a decision on a claim given in accordance with Section 42 of the Taxes Management Act 1970 which was subsequently determined either by the Commissioners or under Section 54 of that Act. But, even if there was no determination of an appeal, a discovery assessment will not be made if the particular point on which the Inspector takes a revised view was, or (as in the *Olin* case, see paragraph 8 above) could be said to have been, the subject of the specific agreement of the final figures for assessment purposes. These circumstances may arise because the figures were agreed before an assessment was made, because the Inspector decided not to make an assessment, or because the Inspector's decision on the claim was accepted.

(iii) No specific agreement: appeal and non-appeal cases

E.13 There will also be circumstances in which the *Cenlon* and *Olin* principles are not applicable. Thus, the particular point on which the Inspector subsequently takes a revised view and considers making a discovery assessment may not have been the subject of a specific agreement or, because the point was not fundamental, cannot be said to have been the subject of a specific agreement (see paragraph 8 above). In these circumstances, a discovery assessment will not be made, provided that the Inspector's original decision, whether on a claim or on the proper amount of an assessment, was based on a full and accurate disclosure of all the relevant facts and was a tenable view, so that the taxpayer could reasonably have believed that the Inspector's decision was correct. And it follows that if the Inspector's original decision was consistent with a view of the law and practice generally received or adopted at the time, a discovery assessment would not be made where, for example, there is a subsequent change in that practice - eg following a Court decision.

Some particular circumstances where discovery assessments will be made

E.14 The application in any individual case of the general principles described in the preceding paragraphs will, of course, depend on the particular facts and circumstances. But there are certain specific circumstances in which there will clearly be no grounds for an Inspector not to make a discovery assessment, ie where

- profits or income have not earlier been charged to tax because of any form of fraudulent or negligent conduct;

- the Inspector has been misled or misinformed in any way about the particular matter at issue;

- there is an arithmetical error in a computation which had not been spotted at the time agreement was reached, and which can be corrected by the making of an in date discovery assessment;

- an error is made in accounts and computations which it cannot reasonably be alleged was correct or intended, eg the double deduction from taxable profits of a particular item (say group relief).

ANNEX F
(para 3.32)

SOME FURTHER COMMENTS ON "DISCOVERY"

F.1 In paragraphs 3.5.8 to 3.5.11 of the Report of the Keith Committee, the Inland Revenue's position on the practical application of the law of discovery was discussed, notably in the light of the decision in *Cenlon Finance Co. Ltd* v *Ellwood (HL (1962) 40 TC 176).*

F.2 The Revenue's views on certain aspects of discovery are set out in Annex E. Pending further judicial guidance on the issue, it is the opinion of leading counsel that the Revenue's interpretation of the *Olin Energy* decision as stated in Annex E is too narrow i.e. the decision could apply even where the point at issue is not fundamental to the agreement of the relevant figures, provided certain other conditions are satisfied (- see next paragraph). Nevertheless, members should be aware of the Revenue's views.

F.3 Thus, it is counsel's view that the Revenue could not raise a new assessment in any case where all such facts as it is reasonable to regard as relevant to considering the point at issue were disclosed and either:

(a) the particular point had previously been raised expressly by the inspector, the taxpayer or the taxpayer's agent; or

(b) the point was so clearly presented that an "ordinarily competent inspector" would have or ought to have taken it into account.

ANNEX G
(para 3.58)

REQUESTS FOR GUIDANCE FOLLOWING MATRIX SECURITIES TEXT OF LETTER DATED 3 JUNE 1994 FROM MR L J H BEIGHTON CB DEPUTY CHAIRMAN OF THE INLAND REVENUE

(Reference may also be made to the Inland Revenue Code of Practice 10: "Information and Advice".)

Requests for Guidance: Matrix Securities

From correspondence, discussion and press comment it is clear that there is some uncertainty following the speeches in the House of Lords in the Matrix Securities case, particularly concerning the extent to which taxpayers can rely on guidance provided by the Revenue. It may be helpful if I comment briefly on the position, as we see it, in relation to the provision, by the Revenue, of 'non-statutory' guidance.

There are two things to say about the Matrix Securities case. First, it seems to us that, in the end, the Matrix case broke little new legal ground; for all their Lordships, whatever the individual differences in their reasoning, the case involved the application of established law (or legal principle) to the particular facts.

Second, however, the case does provide further endorsement at the highest level of MFK and the guidelines set out in that case. In particular, the case underlines the need for complete frankness in circumstances where taxpayers expect to rely on guidance given by the Revenue; disclosure must be full, accurate and fair as to the facts and the complete context in which the ruling is sought.

My letter of 18 October 1990 (copy attached) therefore holds good; we would not wish to withdraw the help we have undertaken, in certain circumstances, to give. Indeed, as you will have seen from the recent Press Release on Rulings, we plan to build on the proposals for a post-transactions rulings system and in due course issue a consultative document exploring the options for an advance rulings system. In the meantime, we are working on a Code setting out our present practice on the provision of advice to taxpayers. We shall wish to seek your views on a draft of that code in a few months' time.

I have been asked whether, following Matrix, taxpayers and their advisers are expected to judge for themselves the appropriate level of Revenue official to whom they should address requests for guidance. It seems to me, on the basis of the case, that the question crucially arises where those seeking Revenue guidance are already aware of views held within the Department contrary to the confirmations being sought. That fact cannot be ignored if people are intending to rely on the advice they get; apart from that there is little to add to what I said in my letter of 18 October 1990.

In the ordinary way, it may be appropriate to write to the Inspector of Taxes who handles the affairs of the taxpayer concerned; but if it is known, for example, that Head Office have recently been considering the issue the appropriate course would be either to write to the relevant Inspector, pointing out the Head Office interest and the need for its clearance or, alternatively, to Head Office direct. In either event an answer should not be sought in an unreasonable time, bearing in mind the complexity of the issues involved and the volume of material to be examined.

Similarly, I have been asked how far taxpayers and their advisers are expected to go in disclosing not only the facts but also the main legal issues arising in particular circumstances. In answering that point I would refer back to my letter of 18 October 1990 when I said that we will provide guidance in certain circumstances and in particular where the operation of the law is uncertain. We are not setting out to give our comprehensive blessing to transactions and schemes put to us but rather responding to the uncertainties in the minds of taxpayers and their advisers on the specific points on which guidance is sought. By definition, therefore, it will invariably be appropriate to spell out those uncertainties and the legal issues on which comfort is being sought as well as it being made clear for what purpose the ruling is required.

I hope this letter will be helpful as you provide advice for your members on the implications of the Matrix Securities case; and I have no objection if you wish to circulate this letter to them. We shall be reproducing it in Tax Bulletin.

TEXT OF LETTER DATED 18 OCTOBER 1990
FROM THE INLAND REVENUE

You may recall that in April 1986 my predecessor, Barry Pollard, wrote to you and to other professional bodies saying that he had advised Inspectors of Taxes at Head Office that they should respond to requests for information or guidance from practitioners only if the enquiry involved recent legislation or changes in practice. The background against which this change was being made was the continuing loss of experienced Inspectors from the Department and the priority which we had to give to giving advice for policy purposes and to local offices.

We have been reviewing experience over the four years since Barry Pollard wrote, particularly in the light of the judgement in the case of MFK Underwriting Agents [1990] 1 All ER 91. One of the factors which lay behind the matters in this case was the pressure on Head Office Inspectors at the time in giving advice to practitioners. With the benefit of hindsight the case can be seen to have justified to the hilt the change which we made in 1986. Nevertheless we are, of course, aware that the professional bodies were unhappy that we had changed the practice and with that in mind we have recently looked at it again.

In considering this matter we have found that the practice has varied a little and that in some areas we have been able to respond to a slightly wider range of questions than Barry Pollard indicated we would. We have therefore now told our Head Office staff that they should be prepared when they can to answer requests for guidance on the Revenue's interpretation of tax law, not only where they involve the interpretation of recent legislation, statements of Practice and other published information, but also in cases where there is a major public interest in developments in an industry or in the financial sector but where the operation of the law is uncertain. In addition, local Inspectors of Taxes will of course continue where practicable to inform practitioners about the Revenue's interpretation of tax law as it applies to any case which falls within the responsibility of that office.

In no case, however, whether at Head Office or local Office, would a member of the Department seek to advise a taxpayer or a practitioner on the arrangement of a person's own affairs: that must remain the responsibility of his professional advisers. Still less of course could we advise in the area of tax planning.

Where guidance is sought, the enquirer will doubtless bear in mind the principles set out by Bingham LJ in the MFK case. In addition to providing details such as the tax district and the reference, the enquirer should bear in mind that if he wishes to rely on Revenue guidance he must

a. put all his cards face upwards on the table;

b. indicate the guidance sought;

c. make it plain that it is fully considered guidance that is being sought; and

d. indicate the use which it is intended to make of the guidance, and in particular whether he proposes to tell others of it.

Where guidance is given it should not be relied on to the extent of any qualifications it contains. Moreover the actual application of the law will depend on the precise way in which the transaction is carried out and of course on the precise terms of the law at the time.

There may occasionally be cases, in particular where a representative body would find it helpful to be given an informal view of the interpretation of new legislation, where it would be appropriate for a reply to be given on an explicitly non-binding basis. Such cases will of course be quite different from Statements of Practice on the one hand or the more formal guidance with which this letter is otherwise concerned.

I hope you will find this letter helpful. As you know, the Revenue have for a long time - as confirmed by the Taxpayer's Charter - been anxious to help taxpayers know their rights as well as their obligations. It was welcome that in the MFK case the Court did not dissent from our view that we should do so where possible, subject to the clear rules which Bingham LJ enunciated as necessary if advice is sought on which the Revenue is to be bound. Even with the welcome reduction in the loss of fully trained Inspectors to the professions and to industry, there remain limits on what we can do, but within these limits we shall continue to develop our services to the public.

ANNEX H
(Para 4.6)

DISCOVERY AND DISCLOSURE UNDER SELF-ASSESSMENT

Revenue Press Release dated 31 May 1996

Introduction

H.1 The introduction of self-assessment and the electronic lodgement service (ELS) heralds a new approach to the handling of tax returns, with more realistic filing dates and streamlined procedures. In particular, the new return has been designed to enable full disclosure to be made without the need to send in accounts or computations in most cases. But concerns have been expressed that reliance on the self-assessment return, without additional information, such as accounts, might expose taxpayers to a greater risk of "discovery" assessments under (new) TMA 1970 s.29. This paper addresses the concerns that have been raised during the Revenue's discussions with representative bodies.

Discovery

H.2 New TMA 1970 s.29 introduced by FA 1994 s.191 is designed to reproduce the current mix of law, practice, and concession on discovery set out in the Revenue's Statement of Practice SP8/91 as it applies for self-assessment.

H.3 The foundation of the principle of discovery is that the Revenue should be able to recover tax which has been under-assessed (or over-relieved) where there is fraudulent or negligent conduct or where the Revenue officer could not be reasonably expected to be aware of the under-assessment (or excessive relief) from the information provided in or with the tax return.

Disclosure

H.4 This paper is concerned only with the second of these two aspects, the concept of "disclosure". Where all relevant facts are disclosed to the Revenue, taxpayers can be certain (except in the case of fraud or neglect) they have gained finality at the end of the enquiry period.

H.5 TMA 1970 s.29 sets out the ways in which information is made available for the purpose of making a disclosure. These include providing details in the return or claim, or in any material accompanying the return or claim, for the year in question or the two preceding years. In addition, it is open to the taxpayer or agent to write to the Revenue explaining the existence and relevance of any particular material for the purposes of making an adequate disclosure.

H.6 A change of opinion on information that has previously been made available to the Revenue will not be grounds for a discovery assessment.

The self-assessment return and standard accounts information

H.7 Additional information takes more time to process and store, costs which by extension all taxpayers bear. The new return is designed to enable full disclosure to be made without the need to send in accounts or computations in most cases. Taxpayers and practitioners are entitled to send in additional material if they consider that it adds information of relevance

to the tax liability which cannot be contained within the return. The Revenue will accept any additional information sent in with the return; see para 14 (accompanying documents) below.

H.8 The self-assessment return requires comprehensive information regarding each taxpayer's affairs. With the exception of partnerships whose annual turnover exceeds £15million (see para 11 below), separate accounts and computations are not required to be submitted with the return. Instead specific details, including standard accounts information (SAI), are required within the return.

H.9 The majority of income tax cases involve reasonably straightforward accounts. In these cases the fully completed return and SAI will enable a full and fair picture of the taxpayer's affairs including any business to be presented. In otherwise straightforward cases there may be the odd point of difficulty which needs further explanation. Such aspects may be dealt with by providing extra information within the areas provided on the return.

H.10 In some of the larger or more complex cases the SAI details and the space provided in the return for additional information may not by themselves provide a means of adequate disclosure. The submission of further information, including perhaps the submission of accounts, may be considered appropriate by the taxpayer or agent. Such cases would include, for example large partnerships with substantial turnovers or cases where, although not large, the business is complex - perhaps because it is a highly specialised trade, or where accounts or computations are required for a proper understanding of the figures.

H.11 The SAI will have to be completed in order for the return to be accepted, even when the accounts are submitted. To leave this information to the discretion of the taxpayer would seriously undermine its value to the Revenue. The only exception is for the very largest partnerships (ie annual turnover over £15 million) where taxpayers are required to submit accounts and computations as well as the return instead of completing SAI. This difference in treatment is justified because the Revenue are likely, anyway, to require to see the accounts and computations of these large cases every year, on account of their size and inherent complexity. Tax returns will be considered to be incomplete where, at the filing date, the SAI boxes have not been completed or, in cases where partnership turnover exceeds £15 million per annum, the accounts have not been submitted.

The submission of additional material

H.12 Taxpayers and agents should be aware that the submission of accounts and computations or other documents may not provide protection against a discovery assessment beyond that arising from the submission of the return alone. The information contained in the additional material may have been fully covered within the return or, alternatively, there may be so much material that the Revenue officer "could not have been reasonably expected, on the basis of the information made available to him before that time, to be aware" (TMA 1970 new s.29(5)) of the particular point of liability, unless the taxpayer or agent had explained its relevance. Where voluminous information beyond the accounts and computations is sent with the return, therefore, it is recommended that there should be a brief indication of the relevance of the material.

Electronic lodgement service

H.13 The electronic lodgement service (ELS) will accommodate all the information which may be given on the self-assessment return, including any additional details in the "white space". Furthermore, recent developments in the design of the ELS system mean that the service will be able to cope with substantial amounts of additional information such as accounts or computations should their submission be considered appropriate by the taxpayer or accountant.

Accompanying documents

H.14 The s.29 definition of disclosure includes information in "any accounts, statements or documents accompanying the return". The Inland Revenue consider that any material sent in support of a return "accompanies" the return for that purpose. Although advised that, in strictness, statutory time limits for filing a return apply equally to any documents intended to accompany it, the Revenue will accept that any documents submitted within one month of the return "accompany" it for the purpose of making a disclosure within TMA 1970 s.29 if the return indicates that such documents have been, or are to be, submitted. Where documents have been sent outside that time limit, the Revenue will consider sympathetically any request for them to be treated as supporting the return in question for that purpose.

Conclusion

H.15 It is in everyone's interests that the new self-assessment system enables taxpayers to disclose their affairs fully. The Inland Revenue believe that this can be achieved through the return and SAI, explanations in the space provided in the return for additional information, or the submission of accounts or computations where appropriate. The self-assessment return and the guidance notes will help taxpayers to be aware of matters which should be disclosed and, where there are doubts, taxpayers can consult their tax adviser or the Revenue.

ANNEX I
(para 8.6)

INLAND REVENUE'S POWERS TO OBTAIN INFORMATION

Power to obtain information on appeal

I.1 TMA 1970, Part V contains provisions relating to proceedings before the General or Special Commissioners (detailed regulations are contained in statutory instruments effective 1 September 1994). These cover appeals and proceedings which are to be heard and determined in the same way as an appeal against an assessment. The Commissioners may, before an appeal is determined, give notice to the taxpayer requiring the delivery of such particulars as they may need for the purpose of determining the appeal and to make available for inspection books, accounts or other documents in his possession or power which, in their opinion, contain or may contain information relating to the subject matter of the proceedings.

Power to call for particulars and documents of client

I.2 Irrespective of whether an appeal is pending, TMA 1970 s.20(1) and s.20 (2) enable the inspector or other authorized member of the Board to require a taxpayer by notice in writing to deliver particulars or documents. These must be in the taxpayer's possession or power, and, in the inspector's reasonable opinion, contain information relevant to any tax liability to which the person is or may be subject or to the amount of any such liability. The word 'particulars' is very broad in meaning and embraces questions seeking information about matters impacting on the taxpayer's taxation liabilities.

Power to call for documents from a third party

I.3 TMA 1970 s.20(3) enables an inspector, with the approval of a Commissioner, to obtain a notice demanding the production of documents (but not particulars) from a third party. The documents must be such as are in the third party's possession or power and as in the inspector's reasonable opinion contain, or may contain, information relevant to any tax liability to which the taxpayer is or may have been subject, or to the amount of any such liability.

Power to call for working papers

I.4 General access to papers is given by TMA 1970 s.20A. Subject to the Revenue's obtaining the requisite judicial authority, the inspector can require delivery by a "tax accountant" (as defined) of all documents relevant to the tax liability of any client. The power under s.20A is, however, restricted to those instances where within the preceding 12 months the person concerned has been convicted of a tax offence before a UK court or has had a penalty imposed on him under TMA 1970 s.99: see Section 8.

Restrictions on powers

I.5 Except as regards TMA 1970 s.20(2) notices, an opportunity for voluntary delivery must be given (TMA 1970 s.20B(1)) and there is protection for documents relating to the conduct of a pending appeal (TMA 1970 s.20B(2)).

Falsification etc.

I.6 It is a criminal offence deliberately to falsify, conceal, destroy or otherwise dispose of documents comprised in a notice under TMA 1970 s.20 or s.20A, or in respect of which the opportunity of voluntary delivery has been given under s.20B(1): see s.20BB.

The accountant's position

I.7 TMA 1970 ss.20B(9) to (14) appears prima facie to provide protection from disclosure of a tax adviser's working papers following notices under TMA 1970 s.20(3) or s.20(8A), only to remove it on the other hand by use of an "override" clause. Basically, except where the document is as described in paragraph I.9, the documents protected from disclosure in the accountant's hands are as follows:

(a) audit papers being the property of the auditor and created by him or on his behalf for the purposes of discharging his function under any enactment (as per s.20B(9)(a));

(b) "relevant communications" belonging to a tax adviser (ss.20B(9)(b)); and

(c) those relating to the conduct of an appeal (see s.20B(2)).

The protection in TMA 1970 s.20B(9) to (14) does not apply to notices given under s.20A (power to call for papers of tax accountants).

I.8 Save for TMA 1970 s.20A and s.20C, the Revenue's approach to a tax adviser or auditor for access to working papers would be by way of third party notice under TMA s.20(3) in respect of the investigation of a client. "Communications" has a wide meaning because s.20(3) refers to "documents" under TMA s.20D(3), "document" has the same meaning as in the Civil Evidence Act 1968, Part I. That definition is broad, embracing aides-memoire, tapes and every conceivable noted form of "communication" save for medical and similar records.

I.9 The protections at paragraph I.7 are removed by virtue of TMA 1970 s.20B(11) in respect of any document which contains information explaining any information, return, accounts or other documents which the person to whom the notice is given has, as tax accountant, assisted any client of his in preparing for or delivery to the inspector or the Board.

I.10 In SP 5/90, the Inland Revenue has undertaken to restrict what is otherwise the broad statutory scope of the "override" clause in TMA 1970 s.20B(11) by:

(a) confining the Revenue's access to audit and tax advice papers that contain information showing how an entry in accounts, returns or other information sent to the Revenue was arrived at;

(b) acknowledging that where a document may remain partly protected then that part "may be kept covered up if the auditor or tax adviser wishes" enabling that part to remain undisclosed; and

(c) undertaking that the Revenue will not seek access on a routine basis and will normally do so "only where they have been unable to satisfy themselves otherwise".

I.11 Various other provisions of the Taxes Acts also impose obligations upon the taxpayer to provide information, for example those listed in the table of provisions included in s.98.

I.12 In summary, the Revenue is only entitled to obtain from a tax accountant "any document which contains information explaining any information ..." (TMA 1970 s.20B(11)) as given to the Inland Revenue in one form or another, either by the client or the accountant, and which the accountant helped to prepare or to deliver to the Revenue.

Search and seizure warrant

I.13 TMA 1970 s.20C enables an officer of the Board of Inland Revenue to give information privately on oath to a Circuit judge (sheriff in Scotland or county court judge in Northern Ireland) that "there is reasonable ground for suspecting that an offence involving serious fraud in connection with, or in relation to, tax is being, has been or is about to be committed and that evidence of it is to be found on premises specified in the information ...". Where a judge is satisfied with the information given, he will grant a s.20C search and seizure warrant. This enables the Revenue to gain unfettered access to papers held by anyone other than those which are in the possession of a lawyer and to which a claim to privilege could be maintained. It is an offence for any person to impede the lawful execution of such an order. It is very important, therefore, that members consider carefully the content of working papers created by other professionals and held on members' premises. The point is that documents containing evidence of fraud may be innocently sited on a member's premises which could, in those circumstances, be raided.

Documents of unnamed taxpayer

I.14 Under TMA 1970 s.20(8A) the inspector may, with the consent of a Special Commissioner, require of any person documents relating to an unnamed taxpayer. The Revenue have stated that the object of this subsection is to ensure that they may obtain the relevant documentation from a practitioner where they believe that there has been tax avoidance generally or a particular legal avoidance scheme is being peddled. Subject to there being reasonable grounds, documents may be required other than those protected by legal professional privilege: see paragraphs 2.14 to 2.21.

Foreign tax authorities

I.15 Double taxation conventions between the United Kingdom and foreign states usually include provision for the disclosure of information between tax authorities. In addition a number of EC Directives which provide for mutual assistance between Member States have been enacted into UK law.

Self-assessment enquiries

I.16 The Revenue powers to obtain documents for the purposes of certain enquiries in TMA 1970 s.20 remain unchanged but there are new TMA 1970 ss.9A, 11AB and 12AC relating to enquiries into the self-assessment returns.

I.17 New TMA 1970 s.19A enables the issue of a notice by an officer of the Board for the production of documents, accounts or other particulars to back up entries in the return. S.19A deals also with the form in which the evidence may be provided and the appeal mechanism leading if necessary to a hearing before the Commissioners. TMA ss.11AB and 19A will not apply to corporation tax until 1999 at the earliest.

ANNEX J
(para 9.18)

CONFIDENTIALITY IN VAT MATTERS

HM Customs' Statement of Practice dated 19 March 1993

J.1 As part of our continuing commitment to trade consultation and assisting the taxpayer wherever possible, we entered into discussions with the Tax Faculty of the Institute of Chartered Accountants in England and Wales, the Institute of Taxation and the VAT Practitioners' Group on the question of Tax Advisers and Confidentiality of VAT Matters. The following Statement of Practice is the result of those discussions.

J.2 VAT leaflet 700/47/93, available from local VAT offices, also reproduces this Statement of Practice.

Introduction

J.3 This statement outlines the legal powers and practice of Customs concerning access to business records and information. It has been issued after consultation and agreement with the Tax Faculty of the Institute of Chartered Accountants in England and Wales, The Institute of Taxation and the VAT Practitioners' Group, and deals with the position of tax advisers' confidential advice and opinion. A tax adviser (who need not be professionally qualified) is any person appointed by a client either directly by the client, or indirectly via another tax adviser, to give advice on the client's tax affairs.

Customs' Responsibilities

J.4 Customs are responsible for the proper management and collection of VAT in the United Kingdom. VAT is a self-assessed tax and in order that Customs' officers can determine whether or not a trader has properly accounted for the tax, they need to have access to his/her business records and accounts. Visits for control purposes are generally made by appointment during business hours, and usually to the trader's principal place of business.

J.5 Customs' practice is to deal direct with the trader, and in this respect may differ from that of the Inland Revenue. If it is the wish of the trader and the tax adviser and does not result in unreasonable delay, Customs welcome the involvement and assistance of the tax advisers, and accept that mutual benefits arise. However, the ultimate responsibility for the accuracy and timely submission of VAT returns rests with the person who is registered for VAT.

Tax Advisers' Guidelines

J.6 The Institute of Chartered Accountants in England and Wales and the Institute of Taxation each have professional ethical guidelines and lay down the procedures that members should follow, and the advice that they should give to clients, when defaults or unlawful acts concerning VAT are suspected. In the case of the ICAEW this is dealt with in the Members Handbook at part 1.306 paras 105-126[1]. Tax advisers who are not members of the ICAEW or the CIOT may wish to follow the guidelines of either body.

Customs' Powers and the Law

J.7 Customs' powers concerning the provision of information and the keeping and production of records and accounts are set out principally in the Value Added Tax Act 1983(2), Schedule 7 (as amended), and The VAT (Accounting and Records) Regulations 1989 (SI 1989/2248)(3) which are described by Customs' in Section 8 of VAT Notice 700. This notice is issued to all VAT registered persons.

J.8 Persons concerned (in whatever capacity) in the supply of goods or services in the course of furtherance of a business or to whom such a supply is made, and persons concerned (in whatever capacity) in the acquisition of goods from other Member States or in the importation of goods from places outside the Member States, in the course of furtherance of a business, are required by law to provide information relating to the goods or services or to the supply, acquisition or importation as Customs' reasonably specify, and to produce for inspection documents relating to the goods or services or to the supply, acquisition or importation.

J.9 Notwithstanding their legal powers, Customs' policy is to seek access to information and records selectively and on a voluntary basis, and their formal powers are used only where all else fails.

Customs Confidentiality

J.10 Customs are aware that a great deal of the information to which they have access is of a confidential nature. They take great care to ensure that respect for confidentiality is maintained.

Categories of information

Information relating to goods or services, or to the supply, acquisition or importation.

J.11 Customs need access to information relating to goods or services or to the supply, acquisition or importation, to enable them to check the amounts of VAT payable/recoverable by businesses, and to ensure that such VAT liabilities are accounted for at the correct time. See paragraph 64(a), part VIII of Notice 700 (The VAT Guide).

Confidential Advice

J.12 As part of their services to clients, tax advisers communicate with clients or other tax advisers for the purpose of giving or obtaining opinion or advice from clients' past or future VAT affairs. Such communication can include notes of meetings and telephone calls, internal memoranda, letters and faxes and management letters. Depending on their content, such communications may or may not be subject to Customs' statutory powers of access.

Notes (not part of the Statement of Practice)

(1) Superseded by these guidelines.

(2) Now in VATA 1994, Schedule 11 (as amended).

(3) As amended.

For a note on Customs' powers to obtain information see Annex K.

J.13 Customs recognise that tax advisers have a duty of confidentiality to their clients. Whilst the duty of confidentiality may sometimes be over-ridden by legal requirements, Customs will not normally request the tax adviser or the trader to produce a communication relating to confidential opinion or advice of the type described above. Auditors' working papers and management letters, except to the extent that they contain information relating to goods and services or supplies, acquisitions or importations, fall into this category.

Mixed information

J.14 In those cases where a document, such as a management letter or an auditor's working papers, contains both information of the type set out under Information Relating to Goods or Services and advice of the type set out under Confidential Advice, Customs will normally accept an extract from the document, supported by a written statement from the tax adviser or auditor that in his opinion Customs do not have the power to see the other part or parts of the document. The extract would include information about the origin of figures in accounts and returns and other information submitted to Customs, or the relationship of those figures with the books and records of the trader. In this context, tax advisers might find it beneficial when corresponding with clients to distinguish between the information set out under Information Relating to Goods or Services and confidential advice, perhaps sending separate correspondence depending on the category into which they consider the material falls.

J.15 In some instances Customs may request access to material to which they consider they may not have statutory power of access. When making such a request, Customs will make it clear to the trader that they are asking for something which may not be demandable as of right. However, the trader or his tax adviser may wish to consider whether access could be in the interest of the trader, for example by facilitating the speedy resolution of his tax affairs.

Disputes

J.16 Where there is a dispute about the information or records sought by Customs, requests for access will be made in writing to the trader, stating the reasons why Customs consider that such information is relevant, and the statutory power(s) under which they seek access.

ANNEX K
(para 9.18)

CUSTOMS' POWERS TO OBTAIN INFORMATION

K.1 Customs have extensive powers to require the production to them of information or documents in relation to a supply of goods or services or an acquisition or importation of goods.

K.2 In particular, VATA 1994 Sch 11, para 7(2) states that every person concerned (in whatever capacity) in the supply of goods or services in the course of a business, or in the acquisition of goods from another member State or the importation of goods from outside the Member States shall, as regards that transaction, supply the Commissioners with such information as they may require and make relevant documents available for inspection.

K.3 Paragraph 7(3) empowers Customs to require others in possession of such documents to produce them and this would include members particularly in view of paragraph 7(4) which says that documents `relating to the supply of goods or services' include any profit and loss account and balance sheet. Customs would not normally require a member to produce a letter that gives advice to a client, auditors' working paper or management letter, unless it deals specifically with a supply, acquisition or import as stated above (see Annex I).

K.4 Paragraph 7(2) is obviously required in order to permit Customs to require production of a trader's normal records in the course of a control visit. However, in conjunction with paragraph 7(3) it appears to cover papers held by a professional accountant as well as by the client. Indeed, the words `in whatever capacity' imply that people with only a remote connection with a business can be required to produce documents they hold.

K.5 Customs have outlined in the Statement of Practice in Annex J the circumstances when they would normally demand information and the type of information they would require and members should produce the statement to Customs officers if they feel that unreasonable requests are being made.