Analysis

Finance Bill 2021: financial institution notices

Speed read

The Finance Bill contains provisions which, if enacted in their current form, will allow HMRC to issue a new form of information notice, the financial institution notice (FIN), to financial institutions, requiring them to provide HMRC with information relating to taxpayers. Unlike current third party notices, neither taxpayer nor tribunal consent will be needed and there is no appeal process (although judicial review will be possible). This has given rise to concerns that there are inadequate safeguards on HMRC's use of FINs.

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In July 2018, HMRC published a consultation document (*Amending HMRC's civil information powers*) which included different proposals to make it easier for HMRC to obtain information about taxpayers from third parties. Those proposals were criticised for removing important taxpayer safeguards and it was unclear the extent to which they would be taken forward. Then, last July, the government published proposed new legislation introducing reforms along the lines of one of the proposals in the 2018 consultation document, in the form of the introduction of a new type of information notice, referred to in the legislation as a 'financial institution notice' (FIN), that requires financial institutions (FIs) to provide HMRC with information relating to taxpayers.

Despite criticism, these new rules seem set to be included in this year's Finance Act and to have effect from the date it receives royal assent.

The current position

FA 2008 Sch 36 allows HMRC to issue a variety of notices requiring recipients to provide information to it, including 'taxpayer notices' under which taxpayers are required to provide information about themselves and 'third party notices' under which third parties are required to provide information about taxpayers. Importantly, third party notices can only be issued with either agreement of the relevant taxpayer or approval of the tribunal.

A third party notice cannot be appealed by the taxpayer but, if issued without tribunal consent, can be appealed by the third party on the grounds that compliance would be unduly onerous (other than in relation to a requirement to provide information or produce documents forming part of a taxpayer's statutory records).

HMRC considers that the need to get taxpayer or tribunal consent is unduly burdensome and out of step with equivalent foreign rules, with the result that it makes it difficult for the UK to comply with its obligations under international agreements for the exchange of tax information in a timely manner. In the summary of responses to the 2018 consultation ('the response document'), which was published in July alongside the draft legislation, HMRC said that it takes, on average, 12 months to reply to an overseas request when it needs to use a third party notice whereas it should reply within six.

The draft legislation

Clauses 122–124 and Sch 33 of the Finance Bill 2021 make changes to FA 2008 Sch 36, including the insertion of the new rules for FINs.

Requirements of a FIN

Under new para 4A of Sch 36, an officer of HMRC can require a 'financial institution' by notice in writing to provide information or produce a document provided the following conditions are met:

- the information or document is, in the reasonable opinion of the officer, of a kind that it would not be onerous for the institution to provide or produce;
- the information or document is reasonably required by the officer for the purpose of checking the tax position of another person whose identity is known to the officer (the taxpayer) or of collecting a tax debt of the taxpayer. (The ability for HMRC to obtain information in relation to tax debt collection is not limited to FINs. The Finance Bill is amending Sch 36 to allow HMRC to obtain such information using other notices issued under that schedule); and
- an 'authorised officer of Revenue and Customs' has given the notice or has agreed to it being given. The statutory definition of the term is fairly unenlightening (broadly, an officer who is authorised by the HMRC commissioners for the relevant purpose) but HMRC says in the response document that such officers are experienced staff who are not personally involved in the cases they review.

In addition, the FIN must name the taxpayer to whom it relates and HMRC must give that taxpayer a copy and a summary of the reasons why HMRC requires the information and documents. However, HMRC can apply to the tribunal to disapply any of these requirements. The application must be made by, or with the agreement of, an authorised officer. If the requirement sought to be disapplied is naming the taxpayer, the tribunal must grant the application if satisfied that the officer has reasonable grounds for believing that naming the taxpayer might seriously prejudice the assessment or collection of tax. However, if the disapplication sought relates to the requirement that the taxpayer be given a copy of the FIN and summary of reasons, the standard that must be met for the tribunal to be obliged to grant the application is slightly different. In that case, it must be satisfied that complying with the relevant requirement might prejudice the assessment or collection of tax.

If the tribunal disapplies the requirement to give a copy of the FIN to the taxpayer, then further amendments to Sch 36 (which will also apply to third party notices) allow the FIN to include a requirement that the FI not disclose the FIN, or anything relating to it, to the taxpayer or, except for a purpose relating to compliance with the FIN, to any other person. It is therefore not entirely clear the extent to which the relevant

FI would be able to discuss the FIN with its advisers for the purpose of checking its validity.

The non-disclosure requirement lasts for 12 months beginning on the date the FI is given the notice unless before the end of that period HMRC in writing (i) withdraws the requirement, or (ii) extends the period for an additional 12 month period (something that it can do repeatedly). Any such amendment to the time period must be by, or with the agreement of, an authorised officer. The officer can only extend the period if it has reasonable grounds for believing that not doing so might prejudice the assessment or collection of tax.

The restrictions on the use of information notices generally in Sch 36 Pt 4 will apply to FINs, e.g. their non-application to documents subject to legal professional privilege.

What is a 'financial institution'?

A FIN can only be issued to a 'financial institution'. This term is defined widely for these purposes in Sch 36 new para 61ZA, catching:

- a financial institution under the OECD's common reporting standard for automatic exchange of financial account information (CRS), as it has effect from time to time, other than an institution that is only within that definition because it falls within section VIII (A)(6)(b) of the CRS. The explanatory notes to the Finance Bill say that this exception is to ensure that family trusts and charities are not within scope. However, section VIII(A)(6)(b) is not limited to just those entities, but, rather, catches (broadly speaking) externally managed investment entities. That being said, even if externally managed funds are excluded from the FIN provisions, that would not exclude their managers, so information about fund investors could potentially be the subject of a FIN issued to the fund manager; or
- a person who issues credit cards.

Can a FIN be appealed?

If the requirements for the issue of a FIN outlined above have been met, there is no right to appeal the issue (although the third party can appeal against any penalties charged for failure to comply with the FIN). A taxpayer could make an application for judicial review of HMRC's decision to issue a FIN but that process can be costly and time-consuming and it is likely to be hard for a taxpayer to meet the threshold required to overturn the decision. In addition, the interaction between a taxpayer's application for judicial review and the FI's compliance with the notice may not be straightforward, especially if the FIN includes a requirement that the taxpayer not be notified.

Taxpayer safeguards

In its review of the 2018 consultation, the House of Lords Economic Affairs Finance Bill Sub-Committee ('the HoL Committee') saw tribunal oversight of HMRC attempts to obtain information from third parties as an important taxpayer safeguard. It considered that HMRC had not offered a convincing rationale for its removal and recommended that the proposals be withdrawn until a consultation could take place on better targeted rules.

As the response document indicates that many respondents shared the same concerns as the HoL Committee, it is disappointing that the draft legislation follows a similar approach to the 2018 proposals for FINs. A new feature is a requirement on HMRC to report the number of FINs issued during each financial year together with such other information (if any) as the Treasury may reasonably require, with the information contained in the report being laid before the House of Commons. However, whilst such a report may give an indication of systemic overuse of FINs, it will not assist a taxpayer or FI in relation to any particular enquiry.

Although the basic requirements for the issue of a FIN can be seen as similar to those for a third party notice, it would appear that the balance of power has potentially been significantly shifted in favour of HMRC. This is primarily because the lack of tribunal oversight and appeal mechanism means that HMRC is being relied upon to scrutinise itself effectively, and it would not be surprising if an 'authorised officer' took a more HMRC-friendly approach than the tribunal would have done.

FIs will be interested in how HMRC apply the non-onerousness requirement. Currently, a non-tribunal approved third party notice can be appealed on the grounds that compliance would be unduly onerous. FINs will have no such appeal right. Instead the question will be whether, in the reasonable opinion of the HMRC officer giving the notice, the information or document is of a kind that it would not be onerous for the FI to provide. Without knowing the particular FI's internal information storage systems, it is hard to see how HMRC can assess this and it is therefore hoped that HMRC looks to work with FIs to understand what they can and cannot easily provide.

Certainly, the HoL Committee was concerned that the current FIN proposals do not contain adequate safeguards, with its report from December last year stating (at para 121): 'The civil information powers proposals are poorly targeted, disproportionate in their effect on UK taxpayers and lacking necessary safeguards and rights of appeal. They remove safeguards for taxpayers and financial institutions which prevent arbitrary use of the information powers, and are not supported by the evidence.'

What will the new rules mean in practice?

The number of information requests from other jurisdictions in relation to which HMRC sought tribunal approval to issue a third party notice has been very low (49 for 2019/20). However, that may reflect the fact that the spectre of the tribunal process itself discouraged HMRC from seeking to issue such notices. Therefore, past behaviour in relation to third party notices may well not be a useful guide to HMRC use of FINs. However, it may be that some comfort can be taken from recent warm noises by the government in relation to oversight in response to the HoL Committee report and the government's impact assessment on the measure which indicates that HMRC expects FINs to impact on only about 20 FIs, albeit that does not reveal the number of FINs that HMRC expects to issue to those FIs.

Accordingly, until HMRC starts issuing FINs it is hard to know the extent (if any) to which FIs will receive more information requests than currently or ones that it is unlikely HMRC would previously have made. However, under the new rules, the potential is there.

In particular, it will be interesting to see whether HMRC confines the use of FINs just to information requests from foreign jurisdictions (i.e. the purported target of the new rules). This issue may be something of a slow burn, with HMRC's use of FINs initially being fairly limited but, over time, increasing as staff changes mean that its memory of the reason for their introduction fades and officers become more familiar with (the ease of) using them.

Given that so much of the FIN mechanics turn on HMRC's internal decision-making, it is hoped that it is prepared to work collaboratively with FIs and to provide clear guidance, ideally in advance of the new regime coming into effect. ■

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- The proposed 'financial institution notice' (S Osprey, 4.8.20)