

# Tax Representation



## TAXREP 06/09

### MEETING THE OBLIGATIONS TO FILE RETURNS AND PAY TAX ON TIME: CONSULTATION RESPONSES AND REFINED MODELS

*Memorandum submitted on 13 February 2009 by the Tax Faculty of the Institute of Chartered Accountants in England and Wales in response to a document published by HM Revenue & Customs in November 2008.*

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The Tax Faculty of the Institute of Chartered Accountants in England and Wales

TAXREP 06/09

Meeting the obligations to file returns and pay tax on time: consultation responses and refined models

## MEETING THE OBLIGATIONS TO FILE RETURNS AND PAY TAX ON TIME: CONSULTATION RESPONSES AND REFINED MODELS

### INTRODUCTION

1. We welcome the opportunity to comment on the refined proposals published by HMRC on 24 November 2008 in connection with 'Meeting the Obligations to File Returns and Pay Tax on Time' at [http://customs.hmrc.gov.uk/channelsPortalWebApp/channelsPortalWebApp.ortal?nfpb=true&pageLabel=pageLibrary\\_ConsultationDocuments&propertyType=document&columns=1&id=HMCE\\_PROD1\\_028673](http://customs.hmrc.gov.uk/channelsPortalWebApp/channelsPortalWebApp.ortal?nfpb=true&pageLabel=pageLibrary_ConsultationDocuments&propertyType=document&columns=1&id=HMCE_PROD1_028673). We are particularly pleased to note that feedback given orally and in written representations has been taken into account in the revised proposals.
2. There are currently fifteen different penalty structures that apply to returns that are filed late and to tax that is paid late. The consultation reconsiders the circumstances in which taxpayers should become liable to civil penalties when they do not meet the basic obligations to file returns on time and to pay the tax due on time.
3. It also considers how HMRC can better support taxpayers better to help them meet their obligations and what form an aligned set of safeguards for penalties should take.
4. New, aligned penalty structures for late filing and late payment of all taxes and duties administered by HMRC were considered in the June 2008 HMRC consultation 'Meeting the obligations to file returns and pay tax on time'. The ICAEW responded to this consultation in its TAXREP 72/08 and subsequently attended a workshop in September on the same subject.
5. The current consultation explores the key themes that emerged from the June consultation and seeks views on modifications made to the proposed penalty structures and relevant safeguards.
6. The design principles underlying the penalty structure are that it should:
  - Influence behaviour;
  - Be fair and proportionate; and
  - Be effective and set out in legislation.
7. Details about the Institute of Chartered Accountants in England and Wales and the Tax Faculty are set out in Annex A. Our Ten Tenets for a Better Tax System which we use as a benchmark are summarised in Annex B.

## KEY POINT SUMMARY

8. We are pleased to note that the refined proposals have taken into account many of the issues and concerns raised in earlier consultations.
9. The overriding objective of any proposals should be to improve tax compliance. We are concerned that these proposals may be seen as a further step down the road to a 'penalty based' culture which may not have the desired effect of improving compliance and could alienate taxpayers.
10. We welcome confirmation that these proposals are not intended to raise more money because these rules will need to be implemented with considerable care and understanding on the part of HMRC if they are to improve compliance. We are concerned particularly that taxpayers who are generally compliant are not alienated by an oppressive penalty regime that punishes misdemeanours rather than providing help and support aimed at encouraging them to get it right next time.
11. Our key points are therefore:
  - a penalty will only influence behaviour if taxpayers know what they are meant to do and are in a position to fulfil their obligations;
  - HMRC needs to provide better support to taxpayers and to identify better ways to communicate with taxpayers – merely putting notices on its website is not enough;
  - there are strong arguments that no one should pay a penalty for the first default for either submitting a return or paying tax late;
  - taxpayers should have the opportunity to have penalties suspended in all situations, not just where time to pay has been requested;
  - penalties in respect of PAYE need to be considered further before they are finalised so that penalties are charged on the appropriate amount;
  - where the obligation to pay PAYE is monthly, the obligation is relatively more onerous and there should not be a penalty until there have been two occasions of late payment in a tax year;
  - penalties levied a long time after the event (as proposed for late in-year PAYE payments) will not be an effective deterrent; and
  - Inheritance tax (IHT) returns should be excluded from these provisions;
  - obtaining more information from all employers to help identify the non-compliant places a disproportionate administrative burden on the compliant;
  - penalties for partnership returns are not considered to be fair or proportionate and should be reviewed

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## GENERAL POINTS

12. If taxpayers are to be encouraged to meet their obligations to file returns and pay tax on time, there is a strong need for improved, ongoing targeted and clear information (as to what penalties will be levied and when), and for support so that taxpayers are fully aware of their obligations, how to go about them and how to address any problems they encounter. This is an on-going education process which is needed to help compliance.
13. HMRC should explore using email and texts as well as letters to communicate to taxpayers essential time sensitive information, particularly where the taxpayer's ignorance of the matter will result in a penalty. In short, for all taxpayers to become aware of their obligations, HMRC needs to use a variety of communication methods and, equally importantly, to get the messages across clearly on a timely basis.
14. The importance of communicating essential information can be illustrated by a recent example where this was not done. The publicity relating to filing returns online by 31 January did not highlight key facts. In order to file online, taxpayers needed to register online for a user ID and PIN well in advance of the filing date and then activate the PIN promptly. Many taxpayers were therefore frustrated at the end of January that they were unable to submit their tax return online without these and as a result would incur a penalty.
15. We recognise that in order to fund Government expenditure, HMRC needs to collect the taxes due on a timely basis. Late payers will generally fall into two groups: those who cannot pay on time and those who choose not to pay on time. The latter group includes those who do not take sufficient care to ensure that they pay on time as well as those who deliberately do not do so. Any penalty regime needs to deal with all these taxpayer behaviours.
16. We note from paras 4.6 to 4.12 that HMRC has introduced initiatives to support taxpayers and should be interested to learn how the effectiveness of such initiatives is being monitored and evaluated. In our view, appropriate guidance and support are an essential and very important part of any strategy to improve compliance of taxpayers with their obligations.
17. The proposed penalties on taxes paid late are in effect the same as the existing late payment surcharges. There may be merit in such penalties being called late payment surcharges to distinguish them from late filing penalties.

## ANSWERS TO QUESTIONS POSED

*Question 1: Do you agree with the findings of the internal and external research presented above? Is there any other analysis or evidence that you could share with HMRC regarding penalties or tax debts?*

18. A penalty will only influence behaviour if taxpayers know what they are meant to do and are in a position to comply with their obligations.

19. We have not undertaken any qualitative or quantitative research of our own but the comments made in Chapter 2 seem to reflect the feedback we have received from our members about client behaviours.
20. Members confirm that the existence of a penalty or a surcharge for late filing or late payment influences the behaviour of many clients. The existence of a penalty seems to be more important than the absolute amount of that penalty because clients do not like to suffer any financial penalty where it can be avoided. However, for certain taxpayers penalties and surcharges seem not to have any effect.
21. Where taxpayers do not have the funds to pay on time, and they therefore cannot avoid the late payment penalties, such penalties will in no way influence payment behaviour, only add to financial problems. Charging penalties in these circumstances are also likely to foster resentment, particularly for a struggling business where penalties or distraint proceedings may lead to business failure. The resentment may then in turn foster future taxpayer non-compliance which is counter productive to future efficient tax collection.
22. We are told by some members that when their clients are in debt, the response which they receive when they contact HMRC can be varied and inconsistent. As a result, and particularly where previous experience has been negative, taxpayers may be discouraged from approaching HMRC at an early stage when they have difficulties paying tax on time.
23. In some instances the taxpayer may be unaware of an obligation to file a return until well after the due date, for example businesses which write up their books quarterly rather than monthly may exceed the VAT threshold without realising until after the deadline. There are similar problems on the occasions of an inheritance tax charge and for corporation tax returns due for entities tax resident in the UK under various treaty clauses. Such unawareness will mean that the existence of penalties will have no effect on filing behaviour.

*Question 2: Is the proposal outlined above that penalties should be suspended where a taxpayer has entered into a time to pay arrangement with HMRC an appropriate way of supporting taxpayers who have difficulties in meeting their payment obligations?*

24. In our view it is essential that taxpayers are advised that penalties will be suspended where they enter time to pay arrangements. If penalties are not suspended, taxpayers have no incentive to advise HMRC as early as possible of payment problems and, equally importantly, to keep to the agreed payment plan subsequently.
25. Such an approach will also be to HMRC's advantage. Where HMRC is aware at an early stage of payment difficulties and agrees a payment plan, there should be lower collection costs for HMRC and less risk of tax loss. In addition, HMRC will be in an early position to monitor the situation and provide appropriate support.

26. Where, as a result of a change in financial circumstances, taxpayers are unable to keep to their payment plan, we consider that if they approach HMRC to re-negotiate it, the penalties should continue to be suspended. This would show that HMRC is committed to continuing to support, rather than penalise, taxpayers when their circumstances change.
27. Very importantly, the suspension of penalties should not be limited only to time to pay arrangements. Suspension of penalties should be available in any circumstance where suspending the penalty will encourage present and future compliance. This is likely to be the case where the taxpayer was, for example, unaware of their obligations, was unable to file for reasons outside their control or has agreed a basis for future compliance with their obligations.
28. In our view the suspension of penalties would be an effective deterrent to future non-compliance in most situations and more importantly would mean that a one-off lapse on the part of the taxpayer is not automatically punished because, as noted in para 4.25, levying penalties can damage the relationship between taxpayer and HMRC which would be counter-productive.

*Question 3: Are the safeguards proposed appropriate? Is the draft guidance appropriate? What modifications, if any, are required?*

29. An appeal can be expensive in terms of time and money. Where the penalty amount is low, the costs of dealing with the appeal may outweigh any potential benefit. It is therefore important that appeals can be made orally so that costs can be kept to a minimum.
30. One safeguard that we should like to see introduced is that HMRC staff should be required to accept telephone requests for them to check their facts and files. There is a tendency by HMRC staff to ask for such requests to be made in writing which increases costs and introduces unnecessary time delays.
31. We welcome the intention to issue clear guidance such as in Annex D. However, we believe that the illustrations of 'reasonable excuse' are too restrictive.
32. For example, in the case of bereavement (para 9) and sudden serious illness (para 11), the death or illness of a close friend or work colleague will, for some, be so upsetting that they are unable to deal with their obligations. In para 10, the circumstances are limited to 'unforeseeable exceptional event disrupting the postal service' which would imply that posting a communication in good time but it failing to reach the destination for an unidentified reason would not be considered a reasonable excuse.
33. We therefore consider that paragraph 12 should be amended to state that, because everyone's circumstances differ, an excuse will not necessarily be accepted because it seems to fit into one of the stated categories and conversely should not be discounted simply because it does not. It will depend on the individual circumstances of each case.

34. One matter which does concern us is that innocent mistakes which are not considered to fall into the 'reasonable excuse' category will tend to be punished in the case of annual or one off returns whereas for more frequent filing obligations, the first such mistake will not be. We should like to be reassured that penalties will be suspended in the case of such mistakes, particularly because the proposed regime seems to unfairly penalise those with less frequent filing obligations.
35. The illustrative guidance, although giving details on what is and what is not a reasonable excuse, gives no indication of what is considered to be 'unreasonable delay'. This must also be included in any guidance. We would expect the criteria for 'unreasonable delay' as with 'reasonable excuse' to vary according to the taxpayer's circumstances and to recognise that taxpayers have many other commitments and calls on their time in addition to their tax obligations.
36. We note that paras 4 and 20 of Annex D duplicate the same information and we consider that the excluded excuses should be included only on para 20.
37. We should welcome the opportunity to comment on any revised guidance.

#### *Comments on Chapter 4*

38. We are pleased that HMRC recognises that penalties can significantly damage the relationship between HMRC and the taxpayer (para 4.25). This can be the case when the penalty is considered to be arbitrary, for example, the penalty for not submitting a CG41G (Corporation Tax – New Company Details) notification form although the corporation tax return is later filed on time.
39. The fact that relationships are damaged by penalties should make the argument for HMRC suspending penalties wherever appropriate even stronger.
40. Charging penalties as well as interest for late payment of tax is considered by many to be unfair and illogical. However, members observe that the existence of a late payment penalty does, where the taxpayer has the means to pay, tend to encourage payment on time where the taxpayer has the means to pay.
41. Para 4.13 refers to internal review. Under the rules for internal reviews, if HMRC does not notify its decision within 45 days, then the outcome is deemed to be in favour of HMRC. There is therefore no perceived incentive for HMRC to undertake the review of the penalty in a timely fashion. We have been informed that this mechanism was put in place for administrative reasons and the taxpayer is protected as he or she can then move on to a more formal appeal process. However, this does not set up an encouraging system of internal review and taxpayers may view the system as being weighted against them from the outset and offering them less opportunity for a fair hearing. We believe this area should be revisited.

*Question 4: Does the model presented for late filing meet the design principles – fairness, effectiveness and influences behaviour?*

42. Any model will only be fair, effective and influence behaviour where taxpayers are aware of their obligations and the consequences of not meeting them. This applies to all forms of penalties. This is why it is so important for HMRC to continue its programme of educating taxpayers, including potential taxpayers, so they are aware of their obligations and the consequences, as time passes, of not complying or delaying compliance.
43. There should be no presumption that any person will automatically be aware of and understand all the issues which may affect them. Although ignorance of the law is not considered to be a reasonable excuse, it is wholly unrealistic to expect all citizens to be fully conversant with all aspects of tax law. Where a taxpayer is apparently not complying with their obligations, efforts should be made by HMRC, in a variety of ways, to engage with the taxpayer to discuss the matter.
44. We agree with the comments in para 5.4 that a fixed sum penalty immediately a return is late is a useful tool to encourage filing compliance, especially for those who procrastinate. We also concur with the view that further fixed sum penalties are likely to be fairly ineffective.
45. Although we accept the points made in para 5.5 about the removal of the capping of the late filing penalty, we still have concerns about those on low incomes where the penalty may represent a disproportionate amount of net income. We trust that HMRC will instruct staff to make every effort to ascertain whether the taxpayer may have had a reasonable excuse and, failing that, suspend the penalty wherever possible and appropriate.
46. Taxpayers who are owed tax by HMRC will probably not consider it fair to be charged a penalty for submitting a return late. Similarly, those who owe very little tax are also likely to consider being charged a penalty for filing their return a few days late to be disproportionate. If such cases are reported in the press, the bad publicity for HMRC is likely to be damaging. This adverse publicity could be avoided if penalties are not applied to the first default in any regime.
47. The continuation of the capping provision for a few more years while the self assessment e-filing system settles down, would also provide a welcome administrative safety net where either HMRC systems has incorrectly recorded the date of receipt of a tax return or there have been other systems delays.
48. Levying penalties for the absence of 'nil' returns is an area which upsets many and which the removal of capping in self assessment will affect. While we accept that HMRC needs to know if there is no liability, if it intends to do this it also needs to make it much clearer to taxpayers that they have an obligation to make a return even where there may be no liability and to make it easy to make such a nil return in a cost effective manner.
49. Para 5.8 explains that HMRC will use the three months following the non filing of a return to contact a taxpayer to remind them that the deadline has passed

and to explain how to obtain help and to set out the consequences of continued delays. We welcome this, especially because as a result of system errors in the past, incorrect e-filing penalty notices have been issued to taxpayers which have resulted in additional costs causing resentment. It is very important that HMRC do use this time effectively and appropriately. We therefore recommend that once deadlines have passed HMRC always send out reminder notices before penalty notices. We would be willing to help HMRC to explore different ways of engaging with different classes of taxpayer during this important period after the first missed deadline.

50. We consider that the approaching imposition of daily penalties may well encourage earlier compliance in many taxpayers than might be the case under the existing regime. However, they will only be effective where the taxpayer is fully aware that such penalties will be levied and of the amounts involved.
51. Communications containing vague statements such as 'you may be charged daily penalties' are unlikely to be as effective as stating 'if we do not receive your return by DD MMM YYYY, you will be charged a penalty of £x for each day it continues to be late'.
52. Provided that our concerns about effective advance communication of the daily penalty regime are addressed in time for taxpayers to contact HMRC, imposing daily penalties during the period three months to six months after the return is late appears to be an acceptable approach to bringing forward the date on which the taxpayer might otherwise have complied.
53. We do however have continued concerns that fixed daily penalties, although simple to understand and communicate, are a very blunt instrument which will impact those on low incomes disproportionately. Some members suggest that the imposition of daily penalties should not be automatic, but simply an option available to HMRC where appropriate.
54. There is also a suggestion that, weekly penalties may be more effective than daily ones. The small increment of a daily penalty for each day of delay, which may be seen as being akin to interest charges, will probably not be effective for those who simply procrastinate. However, the imposition of a larger penalty at slightly less frequent intervals may be more effective because there is a more tangible incentive for submitting a return before the imposition of the next (larger) penalty. We consider that a longer interval than a week for imposing penalties may not be so effective in focussing the taxpayer's mind on completing and submitting the return.
55. As with all penalties HMRC should, where a taxpayer engages with it and makes every effort to bring their tax affairs up to date, consider suspending the penalties provided that future returns are filed on a timely basis.
56. One situation in which penalties do not seem fair and proportionate is that of partnership returns where the penalty is a fixed amount per partner in the partnership. This is perceived by many to be harsh particularly because often, in addition to the penalty for the partnership return, the individual partners are unable to estimate their partnership profit share and will thus inevitably file their personal return late and incur a personal late filing penalty.

57. We consider that where an individual partner has been unable to submit his personal tax return due to the partnership tax return being filed late, the partner will have a 'reasonable excuse' for the late filing and should not incur a penalty. In the absence of this, each partner is being penalised twice for what is effectively a single misdemeanour.
58. Finally, and very importantly, although we note the desire to harmonise the penalty regimes across all taxes we do not consider that it is appropriate to include IHT. Many executors will be bereaved close family or friends of the deceased. They may also be elderly. Tracing all assets and lifetime gifts can be very difficult and particularly so for these people in the difficult circumstances they find themselves. We therefore consider that extending the penalty regime (and Sch 36 etc) to IHT is wrong in principle.
59. The draft guidance already indicates that bereavement is often a reasonable excuse for late filing. Internal guidance should also point out that most executors will only ever deal with one or two IHT returns (generally those of parents or siblings) and accordingly should not be expected to have significant skill, including detailed knowledge of any time limits. We therefore recommend that HMRC should send reminders a month or so before a return is due and offering help in respect of any difficulties being encountered.

*Question 5: Are the modifications to the late filing penalty model, to reflect the frequency of the obligations, appropriate?*

60. The rolling default window has parallels with suspended penalties discussed above. We believe that it is fair that those with frequent filing obligations should not suffer a penalty on the first default. A key aim of any penalty regime should be to encourage future compliant behaviour and not simply to punish the occasional transgression.
61. However, from para 5.24 it appears that with monthly filing obligations HMRC is still proposing a fixed penalty on the first default and we consider this to be unfair, especially as the first default for quarterly filers does not attract a penalty (para 5.15). A penalty should only be charged for 2nd and subsequent defaults in the default period.
62. The proposal for a fixed sum penalty, increasing in amount with the number of defaults in the period, appears easy to understand and to communicate. However, as noted in paras 18 and 42 above, this regime will only be effective if the taxpayer is aware of the obligation and the effect of filing late is communicated clearly and effectively.
63. We consider that there might still be a case for daily fixed penalties, or as suggested above at para 54, for weekly fixed penalties, to be levied for quarterly returns. The intervals between charging the increasing rates of fixed penalty are quarterly and so not as immediate as daily/weekly penalties. However, we recognise that such a structure would not be as simple to communicate and would be more complex to operate. On balance, having the same penalty structure as annual obligations may not be appropriate.

64. Tax geared penalties for late filing of a return can be disproportionate but we accept that for very late filing the threat of more significant penalties may be effective provided that the impending imposition of the penalty is communicated clearly to the taxpayer.

*Question 6: Does the model presented for late payment penalties meet the design principles – fairness, effectiveness and influences behaviour?*

65. Some members still hold the very strong view that the obligation to file and to pay are interlinked and remain unconvinced by the arguments which HMRC put forward (paras 4.22 et seq, 5.15 etc) to support its view that late filing and late payment are separate and unconnected issues requiring a separate penalty framework. .
66. The two are clearly very much related because the return identifies the amount of tax due for payment. It therefore follows that until a return has been prepared the amount of tax due is unknown, except in cases where it might be possible to prepare reasonable estimates. Where there are difficulties preparing the return on a timely basis and estimates are not possible so that the return is late as a result, some or all of the tax may inevitably also be paid late. It seems unreasonable that taxpayers should be punished twice for what is really the same issue.
67. To be reasonable and fair, penalties for non payment must be proportionate to the risk to the Exchequer of the payments not being received at all if the taxpayer delays payment. We do not consider that imposing a minimum level of penalty (para 5.34) meets the fairness principal.
68. Depending on the type of tax owing and the taxpayer, a percentage penalty may be disproportionate. However, provided that the proposed penalty suspension regime is implemented, it would seem to be possible for taxpayers to avoid disproportionate penalties by engaging early with HMRC which has the additional advantages for HMRC already outlined above.
69. In addition, it will not generally be possible to influence the behaviour of those who do not have the means to pay by adding late payment penalties. This will simply compound the problems which the taxpayer is facing. As discussed in paras 25 and 26 above, suspension of penalties and supporting a payment plan is likely to be the best approach in most of these cases.
70. To be effective, the taxpayer needs to be aware of the penalties which will be charged for late payment which requires clear and timely communication of the amounts involved and the timing of their invocation. This is particularly important where the taxpayer has not yet advised HMRC of the liability; any communications about late filing should also make it clear that if the taxpayer has also not paid the tax due, that tax-geared penalties will be levied as well as late filing penalties.
71. Whilst it is clearly right that HMRC should have an effective regime for dealing with late payment of tax, in our view HMRC must focus more closely on implementing effective enforcement procedures for collecting tax which is overdue. Many taxpayers will be much more likely to pay their tax on time if

they thought that HMRC would take prompt and effective action to enforce payment. We recognise that this would take time and resources, but if HMRC demonstrated that it is serious about chasing those who will not pay (and is willing to raise determinations and assessments where necessary) then in the longer term this is likely to have a much greater impact on improving taxpayer compliance.

72. We are pleased to note that in the case of additional tax becoming due, the late payment penalties will apply by reference to the date on which the additional, rather than the original, tax was due (paras 5.32 and 5.33).

*Question 7: Are the modifications to the late payment penalty model, to reflect the frequency of the obligations, appropriate?*

73. In our view, if HMRC insist on separate penalties for filing and for payment obligations, different rolling default periods for the two obligations would be fair but will almost certainly be confusing for taxpayers.
74. The more frequently taxpayers are required to make payments, the more likely it is that, due to unforeseen circumstances which may not be covered by 'reasonable excuse', more than one payment in an annual period will be late. The annual rolling default window would therefore appear unfair because it is likely to penalise those with monthly obligations (twelve opportunities for lateness) more than those with quarterly obligations (four opportunities for lateness). In the interests of fairness, the default period should be for a number of payments rather than a period of time.
75. In addition, it concerns us that once penalties for late filing of returns become tax-gated, the taxpayer may at a relatively early date suffer very high levels of penalty where both the return and the tax are late. We should like a provision to be in place so that penalties in such cases are restricted to one or the other, rather than both penalties.

*Question 8: Is the overall package of penalties suggested for late filing and late payment likely to be effective, fair and to influence behaviour?*

76. The existence of this package of measures will not, in itself, influence behaviour. It needs to be effectively publicised to all and, in particular, the people most likely to be incur penalties. The behaviour of repeat 'offenders' may only start to change when either they or their acquaintances are actually penalised and start telling others. Current HMRC policy of publicising only high profile or high amount cases is not as likely to influence behaviour as publicising 'real life' cases involving ordinary people to which taxpayers relate – 'that sounds like me'.
77. In our view it is much better to influence behaviour using a combination of methods including both 'carrots' and 'sticks', rather than just sticks. Support, communication, approachability, empathy, flexibility and suspended penalties are all desirable to assist in the aim to get taxpayers to pay and file on time. We believe that appropriate use of the suspended penalty regime, perhaps

even automatically for all first transgressions, can be used very effectively to influence future behaviour.

78. Applying the same package of measures across a range of taxes and situations will inevitably have some shortcomings. For example a daily penalty of £50 will have a much more significant effect on a pensioner than on a multinational company. In our view the combination of measures being introduced, with the associated safeguards, could be effective in improving compliance behaviour and will generally be fair for payers of each tax.

*Question 9: Will the proposal for penalties for late payment of in-year PAYE meet the design principles: be fair, effective and influence behaviour?*

79. We are told that late payment of in-year PAYE is a considerable problem for HMRC and it is clearly unfair to those that do meet their obligations for others to go unpunished when they do not do so. Late payers may obtain competitive as well as financial advantage as a result. For this reason we support initiatives to ensure that employers meet their obligations on time, as required by the law.
80. However, it is our view that HMRC could have been far more proactive to date in attempts to improve a situation where 40% of employers apparently pay late. The existing situation, where an employer is generally not penalised in year no matter how frequently it fails to pay on time, and in many cases does not receive any contact from HMRC other than reminders, does not provide any incentive to pay on time.
81. There are proposals that interest should be charged where payments have been made late but that the interest will be calculated after the year end. As noted in our response to the Consultation document on interest, this is not likely to act as a deterrent to late payment because it happens so long after the event on which it is based. Furthermore, the interest rates charged by HMRC may be cheaper than the overdraft or loan facility available to the employer from a third party.
82. We consider that HMRC should be doing more to identify and target persistent late payers and those who pay the total amount due by the end of the tax year having made only small payments during the year followed by a large payment at the year end. Compliant employers want HMRC to do all it can to make others comply. HMRC should use the information on payments that it already holds at its Accounts Offices to risk assess employers and identify employers whose payments do not fit the expected payment profile.
83. However, introducing a penalty regime which is likely to punish those who occasionally pay late the same as those who persistently do so is not likely to be perceived as being a fair approach.
84. Members are also concerned that compliant employers will have to undertake more work in order for HMRC to catch the non compliant. This is why many compliant employers do not support the proposal requiring employers to provide data relating to the payments which should have been made in year. Other members believe that this requirement, once the software has been

amended to produce the figures required, should not be that onerous, for the majority who use computerised systems and do not provide benefits-in-kind or expenses that need to be passed through the payroll.

85. Of course the majority of employers are not large corporates. Increasingly individuals need to operate payrolls for carers, nannies and housekeepers. Such employers are more affected by unexpected personal events which may mean that they pay a day or so late and it would appear disproportionate to punish this if it happened more than once in an annual cycle. We therefore consider that requiring employers to pay eleven of the twelve in year payments on time is not reasonable and suggest that each employer should be allowed two defaults before any tax geared penalties are charged. Similar provisions would be welcomed in respect of the Construction Industry Scheme (CIS) scheme.
86. Some members have indicated that, although they consider it is reasonable to charge interest when payments are made late, they do not support the idea of penalties being charged for late in-year payments of PAYE which is seen as being unduly harsh.
87. There are a number of practical issues in connection with the proposed 'extended P35' proposal, not just in relation to employers who have multiple payrolls, and those who prepare payrolls manually but also because these is often a difficulty in ascertaining the correct amount of PAYE/NIC payable for the pay period.
88. For example, employers will often encounter delays in obtaining the necessary information for overseas employees and for items such as pecuniary liability payments, e.g. home telephone and utility bills, purchases or payment for provision of services by the employee using company credit cards where the 'litany' is neither applicable nor used, and non-cash vouchers not exempt from tax or NIC. Currently for NIC on 'marginal benefits' there is an easement allowing them to be accounted for in a later pay period. If penalties are introduced for late paid in-year PAYE and the rules for charging tax and Class 1 NIC are not changed, this easement will need to be extended and legislated.
89. Further, if payroll of benefits in kind is introduced, the difficulties in ascertaining the right amount of PAYE income tax and NIC will be exacerbated, as the law governing the charges to tax and NIC of many benefits in kind does not allow the quantum of the benefit to be ascertained in time to calculate the tax, NIC and net pay by the normal pay date.
90. Given these issues we recommend that any in-year penalty should be based on the amount of PAYE which was reasonably thought to be due at the time rather than the actual figure ascertained at a later date, once all information that relates to a pay period is available.
91. The above issues will all need to be considered carefully before any proposal is implemented. We suggest that, as a starting point, consideration be given to the premise that employers are deemed to have paid the correct amount and discrepancies are followed up under provisions relating to incorrect returns.

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TAXREP 06/09

Meeting the obligations to file returns and pay tax on time: consultation responses and refined models

*Question 10: Do you have any information or evidence that you can provide about the likely administrative burden of providing an aggregate monthly breakdown at the end of the year? It would also be helpful if you could provide any information on the processes you have for completing the P35 (for example what checks are involved, seniority of staff involved etc).*

92. Although we have not researched this issue, the additional cost of providing the information for those with a single payroll per P35 and a computerised system would, we believe, be limited to the incremental cost of this addition made by the software provider.
93. In other circumstances the amount of time involved will be variable depending on circumstances and may be between fifteen minutes and several hours per P35.
94. In our view the Impact Assessment therefore underestimates the costs. It estimates (on page 3) that one-off costs are 'to be determined' and annual costs will be £3 million to £6 million. Allowing an average of 1 hour per year per employer at a cost of, say, £30 per hour to check and verify the twelve additional figures adds something in excess of £40m to employers' costs. Of this, around £25m would unjustifiably relate to the majority of employers who are already compliant.

AW 13-02-09

## ICAEW AND THE TAX FACULTY: WHO WE ARE

1. The Institute of Chartered Accountants in England and Wales (ICAEW) is the largest accountancy body in Europe, with more than 128,000 members. Three thousand new members qualify each year. The prestigious qualifications offered by the Institute are recognised around the world and allow members to call themselves Chartered Accountants and to use the designatory letters ACA or FCA.
2. The Institute operates under a Royal Charter, working in the public interest. It is regulated by the Department for Business, Enterprise and Regulatory Reform through the Financial Reporting Council. Its primary objectives are to educate and train Chartered Accountants, to maintain high standards for professional conduct among members, to provide services to its members and students, and to advance the theory and practice of accountancy, including taxation.
3. The Tax Faculty is the focus for tax within the Institute. It is responsible for tax representations on behalf of the Institute as a whole and it also provides various tax services including the monthly newsletter *TAXline* to more than 10,000 members of the ICAEW who pay an additional subscription.
4. To find out more about the Tax Faculty and ICAEW including how to become a member, please call us on 020 7920 8646 or email us at [taxfac@icaew.com](mailto:taxfac@icaew.com) or write to us at Chartered Accountants' Hall, PO Box 433, Moorgate Place, London EC2P 2BJ.

## THE TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. **Statutory:** tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. **Certain:** in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. **Simple:** the tax rules should aim to be simple, understandable and clear in their objectives.
4. **Easy to collect and to calculate:** a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. **Properly targeted:** when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. **Constant:** Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. **Subject to proper consultation:** other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. **Regularly reviewed:** the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. **Fair and reasonable:** the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. **Competitive:** tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as **TAXGUIDE 4/99**; see <http://www.icaew.co.uk/index.cfm?route=128518>.