Finance Bill 2018-19 – Clauses 30, 31;
Schedules 11, 12, 13 – Penalties and interest
Response from the Low Incomes Tax Reform Group (LITRG)

1 Executive Summary

1.1 We welcome the opportunity to comment on the draft Finance Bill 2018-19 clauses and schedules in respect of penalties and interest. We have previously responded to a number of consultations on the reform of tax penalties, welcoming the aim of trying to differentiate between deliberate and persistent non-compliers and those who make occasional innocent errors, for whom alternative interventions might be appropriate. We think that largely the regimes provided for by the draft legislation achieve this, and for the most part adhere to HM Revenue & Customs' (HMRC) five design principles for penalties.[1]

1.2 We note that in the Summary of Responses to the consultation on *Making Tax Digital: Interest harmonisation and sanctions for late payment*, it states that previous consultations "identified that simplifying and harmonising … penalties and interest would make tax administration clearer and simpler for taxpayers, ensuring that it was as easy as possible for them to comply with their obligations across taxes."[2] We accept that simplifying and

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1 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/400211/150130_HMRC_Penalties_a_Discussion_Document_FINAL_FOR_PUBLICATION__2_.pdf

2 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/722450/MTD_Interest_harmonisation_and_sanctions_for_late_payment_summary_of_responses.pdf

CHARTERED INSTITUTE OF TAXATION
1st Floor, Artillery House, 11-19 Artillery Row,
London, SW1P 1RT

REGISTERED AS A CHARITY NO 1037771

Tel: +44 (0)20 7340 0550
Fax: +44 (0)20 7340 0559
E-mail: litrg@ciot.org.uk
www.litrg.org.uk

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harmonising penalties and interest makes that regime simpler, but do not believe that it equates to making it easier for people to comply with their obligations. Ease of compliance depends on systems being easy to access and use, processes working smoothly and clear guidance being available. However, we accept that a sensible and clear sanctions system for non-compliance should act as an incentive for people to comply with their obligations.

1.3 In this response we draw attention to concerns about certain provisions within the Finance Bill. Clauses 30(3) and (4) provide for the coming into force of Schedules 11 and 12 and the commencement of different provisions. We note that the implementation date of the new penalty regime for income tax self assessment filing obligations is to be announced in due course. As it is accepted that the proposed points based model is more appropriate than the current regime, we recommend that consideration is given to introducing the new penalty regime for income tax self assessment from 6 April 2020 (assuming it will be introduced for VAT with effect from the introduction of Making Tax Digital for VAT on 1 April 2020), but subject to an appropriate familiarisation period.

1.4 In respect of paragraph 16(4) of draft Schedule 11 which sets out the amount of the penalty due (currently unspecified), and paragraph 6(4) and (5) of draft Schedule 13 which set out the percentage of tax due (currently unspecified), we recommend that HMRC carry out consultation with stakeholders prior to setting the penalty amounts and percentages.

1.5 We think that the two-year time limit for assessments as set out by paragraph 18 of draft Schedule 11 is too long and runs counter to one of the aims of the new penalty regime – to encourage taxpayers who have been non-compliant to become compliant again quickly. In the majority of cases, HMRC will be fully aware of the taxpayer's accumulated points. We think the time limit should be much shorter, therefore, in order to reflect the objective of encouraging a taxpayer to comply with their filing obligations. One option would be to set time limits for assessments that are in line with the time limits for the award of penalty points.

1.6 We think paragraph 23(3) of Schedule 11 and paragraph 15(3) of Schedule 12 should be amended, such that rather than providing for the possibility of HMRC cancelling a liability, they provide that HMRC **must** do so, when withdrawing a notice to file a return.

1.7 Paragraphs 24 to 26 of draft Schedule 11 provide for appeals against penalty points and/or penalties, but make no distinction between the appeal processes for penalty points and those for penalties. While we welcome the fact that taxpayers will be able to appeal individual penalty points as they are awarded, we do not think taxpayers who choose not to appeal individual penalty points as they arise should be disadvantaged. We request confirmation that the legislation ensures that not appealing a penalty point when it arises does not prevent the taxpayer from challenging that point in the event of a subsequent penalty appeal, and that an appeal against a penalty automatically constitutes an appeal against all the penalty points contributing to that penalty, with certain exclusions.

1.8 We think that paragraph 26(2) of draft Schedule 11 should be amended such that either HMRC or the appellant (or both) have the ability to **require** the tribunal to consider and rule

on any or all of the penalty points that contribute to the penalty that is the subject of the appeal. Currently, the provision merely gives the tribunal the power to do so, if it chooses.

1.9 We question whether the *de minimis* amount of the penalty should be the same for deliberate but not concealed behaviour as it is for deliberate and concealed behaviour, as provided for by paragraph 3(3)(b) and (5)(b) of Schedule 12. In particular, we question whether this is proportionate and whether it meets the five design principles for penalties set out by HMRC in *HMRC Penalties: a discussion document*.[3]

1.10 Although the fact that the date of contact with HMRC in relation to a time to pay (TTP) agreement will be taken as the effective date for the purpose of late payment penalties goes a small way to assuaging our concerns, which have otherwise not been addressed, that the 15-day period is too brief a period, we reiterate our strong recommendation that the 15-day period should be increased.

1.11 There are elements of the new late payment penalty regime that introduce complexity, while also ensuring that the regime is as fair as possible. We recognise the inevitability of the trade-off between the two, but recommend that taxpayer guidance should be clear and ensure the regime is transparent, setting out all rights and obligations of both HMRC and taxpayers. For instance, examples setting out potential taxpayer liabilities should include both penalties and interest. Moreover, notifications issued to taxpayers should explain how penalties and interest will be worked out, so that the levels of the second penalty and any late payment interest do not come as nasty surprises.

2 About Us

2.1 The LITRG is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.

2.2 LITRG works extensively with HMRC and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.

2.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the

[3] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/400211/150130_HMRC_Penalties_a_Discussion_Document_FINAL_FOR_PUBLICATION__2_.pdf

administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

3 Clause 30, Schedules 11 and 12

3.1 Clause 30 and Schedules 11 and 12 introduce a new points based penalty regime for late filing and make amendments to the penalty regime for deliberately withholding information from HMRC.

3.2 Clauses 30(3) and (4) provide for the coming into force of Schedules 11 and 12 and the commencement of different provisions. We understand that the intention is for the points based model to apply from 1 April 2020 for VAT filing obligations; the implementation of the new penalty regimes for income tax self assessment filing obligations is to be announced in due course. If the introduction of the new regime is deferred until April 2021 (or later) for income tax, the unsatisfactory elements of the current late submission penalty regime will continue to apply until then. Although the new provisions are meant to apply generally (not just in relation to Making Tax Digital), it appears that the timing of introduction of the new regime is being determined by Making Tax Digital, rather than the principles on which the new regime is based.

3.3 It is disappointing that the introduction of what, in our view, is a more appropriate penalty regime is going to be delayed and piecemeal. We think that consideration should be given to introducing the new penalty regime for income tax self assessment from 6 April 2020, subject to an appropriate familiarisation period.[4] If the decision is taken to delay the introduction of the new regime for income tax, it is imperative that HMRC provide clearer guidance to taxpayers about the penalties they may incur under the current regimes.

3.4 Paragraph 16(4) of draft Schedule 11 sets out the amount of the penalty due (currently unspecified), when a penalty arises, either because the taxpayer is awarded a penalty point which takes them to the maximum number of penalty points or the taxpayer fails to file a return on time and they already have the maximum number of penalty points. We note that further work is being carried out to determine penalty amounts. It is difficult to comment on how proportionate the penalties are without this information and to date there has been no consultation on penalty amounts. We recommend that HMRC carry out consultation with stakeholders prior to setting the penalty amount.

3.5 Paragraph 17 of draft Schedule 11 provides for HMRC to assess a penalty, and sets out the assessment process. Paragraph 18 goes on to specify the time limit for assessments, allowing the period of two years. This extensive time limit seems to run counter to one of the aims of

[4] We recommended a three-year period of freedom from penalties in our response to the HMRC consultation *Making Tax Digital: Tax Administration*: https://www.litrg.org.uk/sites/default/files/files/161107-LITRG-response-MTD-tax-administration-FINAL.pdf

the penalty points regime – to encourage taxpayers who have been non-compliant (for whatever reason) to become compliant again quickly. In the majority of cases, HMRC will be fully aware of the taxpayer's accumulated points, and therefore the time limit should reflect the objective of encouraging a taxpayer to comply with their filing obligations. One option would be to set time limits for assessments that are in line with the time limits for the award of penalty points, as set out in paragraph 6 of draft Schedule 11.

3.6 Paragraph 23(3) of draft Schedule 11 currently reads: "The notice under section 8B or 12AAA of TMA 1970 **may** include provision cancelling liability to the penalty point or the penalty from the date specified in the notice." Given this relates to the withdrawal of notice to file a return, we would have expected this to indicate that the notice **must** include provision cancelling liability to the penalty point/penalty, since there can be no liability to a penalty point/penalty if there is no obligation to file and this should be communicated clearly to the taxpayer.

3.7 Paragraphs 24 to 26 of draft Schedule 11 provide for appeals against penalty points and/or penalties. Paragraphs 24 and 25 make no distinction between the appeal processes for penalty points and those for penalties, so we assume the normal time limits and rules apply to both. We welcome the fact that taxpayers will be able to appeal individual penalty points as they are awarded, if they wish – indeed this was one of our recommendations.[5]

3.8 By the same token, however, we do not think taxpayers who choose not to appeal individual penalty points as they arise (on the basis, for example, that they think they are unlikely to incur further points and by extension an actual penalty) should be disadvantaged. Moreover, if an appeal against a penalty point is subject to the normal appeal time limits, this might result in taxpayers routinely appealing penalty points, overburdening HMRC and/or the tribunals. We think amendments may be required therefore; otherwise, we would welcome confirmation that the legislation does not disadvantage taxpayers who choose not to appeal penalty points as they arise. Not appealing a penalty point when it arises should not prevent the taxpayer from challenging that point in the event of a subsequent penalty appeal, in which that penalty point is relevant. An appeal against a penalty should automatically constitute an appeal against all the penalty points contributing to that penalty, excluding points that have already been the subject of an appeal and determined accordingly, or points that the taxpayer accepts (or has accepted) voluntarily as being valid.

3.9 Paragraph 26(2) of draft Schedule 11 provides that the tribunal "may … affirm or cancel" any penalty point contributing to the penalty that is the subject of the appeal. We think that this paragraph should be amended such that either HMRC or the appellant (or both) have the ability to require the tribunal to consider and rule on any or all of the penalty points that contribute to the penalty that is the subject of the appeal. This would mean that the tribunal's decision would provide certainty on what penalty points remain valid.

[5] https://www.litrg.org.uk/latest-news/submissions/161108-making-tax-digital#toc-tax-administration

3.10 Complications arise from the application of separate points totals to each obligation and the potential for different points totals to apply to each individual taxpayer. We have concerns as to whether HMRC will be able to operate this regime correctly, keep taxpayers up to date on their points total effectively and providing guidance such that taxpayers are able to understand their position. This is especially the case in respect of the transfer of accumulated points when a taxpayer moves between groups of returns in terms of their filing obligations. For taxpayers with more than one filing obligation that falls within the regime or those who move between groups of returns, particularly if they are unrepresented, it will be very complex to get to grips with.

3.11 We welcome the fact that provision is made for points to expire and that the regime will be introduced with a points lifetime of two years (paragraph 7 of Schedule 11), and that the period of life relates to the date of the failure rather than the date when HMRC award the penalty point. Indeed, we recommended that "there should … be a limit on the length of time penalty points can sit on a taxpayer's account" and indicated that "points should 'expire' 24 months after they have been received" in our response to the consultation *Making Tax Digital: Tax Administration*.[6]

3.12 We welcome the fact that the draft legislation sets out time limits within which HMRC must notify a taxpayer of a penalty point – if these are not met, the point cannot be incurred. In order for these time limits to operate effectively, it is essential that guidance is clear, so that taxpayers can tell easily whether or not a penalty point has been charged legitimately.

3.13 We also welcome the fact that HMRC will have discretion not to award a point or charge a penalty if they consider it appropriate in the particular circumstances. We recommended that "HMRC should be given a discretion to issue warning letters instead of penalties in appropriate cases" in our response to the consultation *HMRC Penalties: a discussion document*.[7] This was aimed at dealing with our concerns about the automated penalty regime for self assessment and the extent to which proper use is made of the safeguards of reasonable excuse and special reduction.

3.14 We note that the draft provisions give HMRC the power to introduce secondary legislation to provide for a familiarisation period during which points and penalties will not be charged for late submissions, when they introduce new or amended return obligations. We hope that this will be utilised as it is important not to penalise taxpayers who are trying to be compliant.

3.15 Paragraph 3(3)(b) and (5)(b) of Schedule 12 set out the *de minimis* amount of the penalty for withholding information through deliberate and concealed behaviour and deliberate but not concealed behaviour respectively. In both cases, the draft legislation provides for an amount

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[6] https://www.litrg.org.uk/latest-news/submissions/161108-making-tax-digital#toc-tax-administration

[7] https://www.litrg.org.uk/latest-news/submissions/150512-hmrc-penalties-%E2%80%93-discussion-document

of £300, despite the fact that the percentages of tax liability to be applied in each circumstance are higher (as one would expect) in respect of deliberate and concealed behaviour. We question whether the same *de minimis* amount should apply in each case and whether this is proportionate – in particular, by having the same *de minimis* amount, there is a risk of failing to encourage compliance, which is one of the purposes of the changes to the penalties regime. Moreover, having the same penalty amount does not seem to meet the five design principles for penalties set out by HMRC in *HMRC Penalties: a discussion document*.[8]

3.16 Paragraph 15(3) of Schedule 12 currently reads: "The notice under section 8B or 12AAA of TMA 1970 **may** include provision under this paragraph cancelling liability to the penalty from the date specified in the notice." Given this relates to the withdrawal of a notice to file a return, we would have expected this to indicate that the notice **must** include provision cancelling liability to the penalty point/penalty, since there can be no liability to a penalty if there is no obligation to file, and this should be communicated clearly to the taxpayer.

4 Clause 31, Schedule 13

4.1 Clause 31 and Schedule 13 introduce a new two-tiered penalty regime for taxpayers that fail to pay tax liabilities on time.

4.2 Paragraph 6(4) and (5) of draft Schedule 13 set out the percentage of tax due (currently unspecified), when there is tax unpaid at the end of the 15-day period and/or the 30-day period. We note that further work is being carried out to determine the percentage. It is difficult to comment on how proportionate the penalties are without this information, however, and to date there has been no consultation on penalty amounts. We recommend that HMRC carry out consultation with stakeholders prior to setting the penalty amount.

4.3 We welcome the fact that some of the points in our previous submissions have been taken on board in drawing up the draft provisions. In particular, we welcome the decision of Government to take the date of contact with HMRC in relation to a TTP agreement as the effective date for the purpose of late payment penalties – this takes on board a recommendation made in our response to the consultation *Making Tax Digital: interest harmonisation and sanctions for late payment*.[9]

4.4 The fact that the date of contact with HMRC in relation to a TTP agreement will be taken as the effective date for the purpose of late payment penalties goes a small way to assuaging our concerns, which have otherwise not been addressed, that the 15-day period is too brief

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[8] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/400211/150130_HMRC_Penalties_a_Discussion_Document_FINAL_FOR_PUBLICATION__2_.pdf

[9] https://www.litrg.org.uk/latest-news/submissions/180228-making-tax-digital-interest-harmonisation-and-sanctions-late-payment

a period when one considers that within that time period the following events are likely to occur: HMRC issue the penalty notification; the taxpayer receives the notification and takes time to consider it (including whether it is valid and for the correct amount); the taxpayer takes appropriate action, whether that is arranging for payment, contacting HMRC to propose a TTP agreement, appealing the penalty or seeking advice (whether from a paid adviser or a tax charity) to ascertain the appropriate next step. We reiterate our strong recommendation that the 15-day period should be increased.

4.5 As noted in our response to the consultation *Making Tax Digital: interest harmonisation and sanctions for late payment*, there are elements of the new late payment penalty regime that introduce complexity, while also ensuring that the regime is as fair as possible.[10] We recognise the necessity of the trade-off between the two, but reiterate our recommendation that taxpayer guidance must include both penalties and interest in examples, to ensure transparency and clarity. Moreover, notifications issued to taxpayers should explain how penalties and interest will be worked out, so that the levels of the second penalty and any late payment interest do not come as nasty surprises.

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[10] https://www.litrg.org.uk/latest-news/submissions/180228-making-tax-digital-interest-harmonisation-and-sanctions-late-payment