HMRC Penalties: a discussion document

Management of taxes

01 July 2015

CIOT, ATT and LITRG comment on the HMRC discussion document

The CIOT, ATT and LITRG have responded to HMRC's recent consultation on penalties, which looked at how the Revenue might change the way that these are applied in the move to digital services. It is a stage one proposal to set out objectives and identify options – in other words, to seek views on the policy design and any suitable possible options before consulting later on a specific proposal for reform.

The CIOT view is that HMRC are right to ask fundamental questions about how the penalty regime should work. HMRC's digital strategy is relevant to this, but there are wider concerns reflected in the document and the Office of Tax Simplification's (OTS) recent report, Tax Penalties: Final Report November 2014, about whether the regime is fair and proportionate.

Overall, we think that the focus of the review should be on assisting taxpayers to understand and comply with their obligations and to pay the right tax at the right time. Penalties should be in line with that policy. We believe that taxpayer education is key from the outset.

The consultation document makes several references to the HMRC powers review which ran from 2005 to 2012 and in which the CIOT, ATT and LITRG were heavily involved. Many of the penalties have resulted from that very comprehensive review of HMRC powers. Although we recognise that the move towards the digital delivery of services is one factor that has prompted this review and will affect the way that penalties can be applied in the future, we should not lose sight of the principles that underscored the previous review, learn from that and build on what has been achieved.

Importantly, the previous review of HMRC powers was not just on penalties and powers but on ‘deterrents’ and ‘safeguards’. We think that this consultation ought to be considering these areas too.

The results of our recent survey into HMRC powers indicate that our members perceive that the current penalty regime operates unfairly. This may in part be due to how HMRC are applying penalties and in particular how consistently and fairly they are doing so. Many respondents thought that HMRC were too quick to charge a penalty for a failure to take reasonable care. The view was also expressed that imposing rigidly fixed penalties for late filing of returns might discourage compliance. Our members also felt that it was unfair that habitually compliant taxpayers are penalised for making occasional mistakes, and are not treated any differently from those who repeatedly file or pay late. Where applicable, we used the survey results to help inform the comments in our response to the consultation document.

The CIOT agrees that HMRC should use their increasing digital resources to promote compliance, by adopting a more personalised approach (with proper use of mitigation and suspension). We believe that the provision of targeted support, using HMRC’s increased capacity to analyse taxpayer information before levying a penalty ought to form part of the process. It must be possible to use the digital data in HMRC’s possession to remind most taxpayers of their obligations and the consequences of non-compliance simply and effectively.

We believe communications between HMRC and taxpayers can be improved to provide clarity and encourage compliance. In particular, we are encouraged by the current HMRC initiative to improve the quality of notifications about the VAT default surcharge.

We support the principle of a single penalty system. Such an approach would fit well with the concept of a single account covering all taxes which should enable compliance across all taxes to be managed holistically. It should be noted that many taxpayers will not be able to engage digitally with the tax system for various reasons, including age and disability. It is vital that these individuals are catered for as the digital transformation of the tax system gathers pace.

Finally, one significant reason for taxpayer error is the complexity of the UK’s tax system, even for people on low incomes. The CIOT firmly believes that compliance

could be improved by simplifying the tax system so that taxpayers can better understand their obligations and how to comply with them.

LITRG's response concentrated on the automated regime for self-assessment late filing and late payment penalties. While applauding the aim of the consultation to produce a regime that 'better differentiates between deliberate and persistent non-compliers and those who might make an occasional error for which alternative interventions are more appropriate', LITRG's response noted that the self-assessment penalty regime makes no such differentiation. The result is that many of the penalties that become chargeable are out of proportion to the tax at stake. LITRG make nine recommendations with a view to introducing proportionality and fairness to the regime.

LITRG added that, although improved digital services should make it possible for compliant taxpayers to get things right most of the time, adequate provision must still be made for exceptional circumstances. These might include those in which the digital systems do not work as intended and for taxpayers who are either not comfortable operating in a digital environment or for whom access to computers or the internet is impossible or exceptionally difficult due to age, disability, inability to afford the expense, or inadequate internet access where they live or work. Nobody should experience an inferior service from HMRC because they are unable to access digital technology.

As well as picking up many of the points made above, ATT's response:

- questioned the sustainability of the 'old regime' of tax-geared penalties for earlier years in parallel with the FA 2007 regime;
- cautioned against ignoring the positive but invisible compliance impact of modest levels of automatic penalties;
- suggested that consideration could be given to self-assessment of certain penalties;
- argued that special consideration was required to Donaldson-type situations where a paper-filer could unwittingly be incurring 'daily penalties';
- drew attention to a number of specific concerns about the VAT default surcharge regime;
- warned against a polarised perception of behaviours, noting that adverse changes in customer compliance behaviour are more likely to have been caused by 'life getting in the way' than by a decision to migrate to the dark

side;
- urged consideration of an expanded and more consistent use of suspension of penalties;
- suggested a possible system to deal with ‘short failures’;
- argued against the imposition of penalties in situations like Palau (the recent DIY house builder case) where a claim had been made erroneously but in good faith for HMRC to consider its eligibility;
- observed that digitalisation could create opportunities for HMRC to alert customers to potential non-compliance and to share their compliance record with them; and
- approved consideration being given to cumulative penalty points and suggested the possible use of user-pay tax compliance awareness courses (delivered by non-HMRC tax professionals) in place of financial penalties.

The CIOT’s response can be found here.

LITRG’s response can be found here.

The ATT’s response can be found here.

The HMRC discussion document can be found here.