The CIOT Diploma in Tax Technology: issues with digital compliance

Management of taxes



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The Diploma in Tax Technology by CIOT will be launched in November, responding to the impact that technology is having on the work of tax professionals. We consider the issue of digital compliance and how it is likely to develop. The report was prepared with the assistance of the CIOT Tax Technology Taskforce, chaired by Ian E Hayes.

Key Points

What is the issue?

Changes to the administration of tax have been and are being set. These digital changes affect how tax is computed, how it is charged, how it is paid.

What does it mean for me?

If the data is wrong or there is a fault with the system, whilst the tax liability will fall on the taxpayer or the adviser, there may be cases where there are contractual rights against advisers or software companies.

What can I take away?

Tax professionals must have the tools and the understanding to work efficiently with the new professionals now part of our world: programmers, data engineers and analysts.

HMRC's self-declared ambition is for the UK to become one of the most digitally advanced tax administrations in the world. Making Tax Digital is a key part of the government's plans and is bringing fundamental changes to the way the tax system works. Whilst there has been some slippage in the timing of implementation, this process is continuing remorselessly.

All VAT registered businesses are now required to keep digital records and use software to submit their tax returns (unless digitally excluded). However, Making Tax Digital for Income Tax Self Assessment has been delayed, so it now will be required of self-employed businesses and landlords with annual business or property income (turnover) above £10,000 from 6 April 2024. General partnerships will not be required to join MTD for ITSA until April 2025 (and exclusions for complex partnerships are expected). It remains to be seen whether these deadlines remain unchanged.

The timing and scope of Making Tax Digital for Corporation Tax remains unclear, although its use will not be mandated before 2026 at the earliest; many expect a later date.

Speaking at Speaking at the CIOT's Parliamentary Reception in September, CIOT president Susan Ball addressed the issue of MTD implementation, highlighting some of the related problems. She said: 'While we support digitalisation, the current timetable for MTD for income tax is unrealistic. Taxpayer obligations are not yet clear, approved software is limited (and) the pilot is not yet up to speed. The government should revisit and consider whether a more gradual, phased approach to MTD will ultimately deliver better results.'

Digital compliance

Changes to the administration of tax have been and are being set. These digital changes cover everything from keeping business records, filing with HMRC and ultimately the structure of parts of the tax system. Individuals could move away from once-a-year tax returns to new ways of reporting.

Large companies may now use specialist tax software to link their accounting systems to financial reporting and tax return systems. Some tax systems have built in robotic process automation to reduce human time processing repetitive tasks. Banks and financial institutions have new tax reporting obligations, where digital reports of taxpayers' income are sent globally between revenue administrations. Work continues under the auspices of the OECD in developing additional reporting by platforms. The UK has adopted 'split payments' for certain overseas sellers transacting via platforms, where the platform may withhold VAT and pay it direct to HMRC, rather than requiring the seller to account for VAT directly.

Systems are enhanced to embrace new social needs and social payments. New digital assets previously neither conceived nor understood must be identified, reported and and taxed. Artificial intelligence is on the horizon.

Clearly, the issue of digital compliance – and how it is to be handled – is one of vital importance to tax advisers. They are following the route set by tax authorities globally and HMRC in the UK by primarily using third party produced software.

HMRC is in the process of moving to multiple new enterprise management platforms for managing UK taxes. These new systems enable HMRC to offer for the first time access to taxpayer data both to taxpayers and their agents. Individual taxpayers are likely to be able to access their data and upload information to HMRC via the forthcoming single customer account. However, agents and taxpayers (particularly companies) seeking more complete access to this system will do so by means of software, using one or more APIs. An application programming interface (API) is a way for two or more computer programs to communicate with each other, built into a piece of software for users. HMRC designs APIs to be built into tax software to meet a wide range of needs. MTD-compliant software is checked by HMRC for its ability to file data into their system, and is designed to be purchased by taxpayers and/or their agents. MTD software is either used to keep accounting records, or it needs to be linked to the existing financial records of taxpayers.

Software companies will have used tax advisers when building and updating their MTD software programs, and these professionals will no doubt have instructed the programmers on the critical data required to be collected and reported for tax purposes to HMRC.

When HMRC checks a VAT software program and gives it a clean bill of health for filing purposes, it is **not** saying that by using this software the taxpayer – or the agent, on their client's behalf – will have complied with the tax law underlying the taxpayer's filing requirement. Rather, it is saying that if all the necessary checks have been undertaken and the data collected by the software system is correct, that software system can interact with HMRC to transfer the return information correctly. And that is all.

Risks with digitalisation

Digitising accounting and tax systems reduces some risks, but it gives rise to new types of risk. If the data is wrong or there is a fault with the system, tax may be incorrectly calculated. The correct tax liability, of course, remains with the taxpayer. In some cases, the taxpayer may have contractual rights against the adviser – or the software company.

Certainly, increased transfer of data digitally should reduce the risk of error because there is a reduction in the number of human interface events. However, digitalisation does not eliminate the risks for the taxpayer or the tax adviser, who remain liable for any errors.

Tax systems are human constructs. A new added factor of risk is the construction of the software system, how it has been adapted for use and how the tax elements within it are reflected. Embedding tax software systems into a comprehensive digital accounting and customer relationship management system needs to be carefully engineered and tested. Those responsible do need to have a sufficient knowledge to understand and accept the system when it has been explained to them.

There is an issue of oversight and comprehension of the digital aspects of tax compliance which is vital within project implementation, and failure to fulfil that role makes a taxpayer or agent vulnerable.

Digitalisation now

HMRC is very much in the vanguard of revenue administrations that have grasped the benefits and challenges of digitalisation where there was, and still is, a multi-layered, legacy tax system.

Phase 1 of the Making Tax Digital implementation programme – which required all VAT registered businesses with a turnover in excess of £85,000 to keep records digitally and file their returns directly from software – is long gone. Commercially available programs are available and online filing is the norm. For some, data analysis has become a key tool in understanding their business better.

Tax advisers know from personal experience how much of their professional life is handled by programmed and programmable machines. Today, almost all personal tax returns are submitted digitally, either by entering data on HMRC's online systems, or by using tax return software. Tax agents and their clients have working relationships with tech companies which manage the software systems with the tools to handle historic compliance processes previously dealt with in analogue, non-binary ways.

Digital change Phase 2 is well underway, requiring direct linkage for tax data reporting in all its forms. The biggest non-deliberate threat to digitalisation is human error. The fewer times that data passes through a human interface (otherwise known as the taxpayer, accountant, bookkeeper or tax adviser!), the more reliance can be placed on that data. At present, this is seen within the timelines and reporting schedules of pre-digital reporting, but undoubtedly move closer to real time reporting.

And this will open the door for Phase 3, already being discussed.

Digitalisation in the future

In some countries, instantaneous reporting can allow real time taxation, certainly for indirect taxes, which, allied with the bifurcation of payments, leads to real time tax payments. Whether the UK will adopt transaction level reporting is an open question. New measures will be introduced to handle new digital asset manufactures, sales, leases and shared intellectual property.

There will also be participation in distributed ledger systems, such as blockchain, that record and certify ownership, providing the ability to transfer legal title to real estate, equities and works of art with smart contracts, which have inbuilt tax

assessment and payment systems.

And then there is the global context, minimum level corporate taxes, cross border exchange of information, extraterritoriality, as well as the new world of crypto assets and non-fungible tokens. The path that new tax advisers will tread is exciting in the extreme, but it will only be possible if they have the tools to do the job, and those tools will be digital.

Embracing change

There is a risk that the role tax advisers play will be fractured by ignorance of digital technology, by reluctance to embrace change and by reliance on adapted old systems until it is too late and obsolescence takes over. Digital technology has changed for good how we do things in terms of compliance, recording and communication.

Companies now advertise roles for tax technologists within in-house tax teams and major advisory firms have teams specialising in this area.

For tax advisers, as for any professional facing the challenge of digitalisation, the ultimate and real question is: how do we change? There are several answers, all centred around an awareness of digital technology and an understanding of how it works, how it can be used and how those key professional principles and practices we have fought so long to establish and adhere to can be transposed and embedded within the digital world.

It will not be necessary for tax advisers to do it all but we must have the tools and the understanding to work efficiently with the new professionals coming into our world, the programmers, the data engineers and the analysts. And just as we recognise the need to understand their world, we also see that they too must change and understand the principles and ethics of tax practice.