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## Introduction

Welcome to Chapter 2 of the Penalties for Inaccuracies learning.

This chapter explains how and why you need to establish the behaviour which caused an inaccuracy or under-assessment to occur. It also tells you how you should gather and record the evidence you need to support your views.

### Study Objectives

After successfully studying this chapter you will be able to

- state the four types of behaviour that lead to inaccuracies.
- state for which behaviour types you may issue a penalty
- describe when you would consider a third party penalty
- provide three examples of reasonable care
- state why you need to keep evidence about the inaccuracies and customer behaviour.

### Study Advice

This is the second chapter and should take you around 2 hours to complete. You will need access to the Compliance Handbook (CH) and the Enquiry Manual.

You should also have completed Chapter 1 before working through this chapter.

## 2.1 Establishing Behaviour

It is important that HMRC is consistent and fair when applying penalties. Penalties for inaccuracies can be charged either for inaccuracies in documents, or when someone fails to notify us of an under-assessment.

For inaccuracies in documents, you must determine the behaviour which gave rise to the inaccuracy in the document. This will determine

- whether or not a penalty can be charged  
and
- together with the quality of the disclosure, the amount of the penalty.

For a failure to notify an under-assessment you do not need to establish behaviour; you will only need to consider disclosure. We will look at disclosure in Chapter 3.

## 2.2 The Four Behaviours

Once you have established there is an inaccuracy, you need to determine the behaviour that gave rise to the inaccuracy. There are four behaviour types, and you will need to consider which behaviour gave rise to the inaccuracy.

The four behaviours are

*CH81120 – 60*

1. **despite taking reasonable care**

*CH430000*

2. **careless** – if the inaccuracy is because the person did not take reasonable care

*Para 3 Sch 24 FA  
2007*

3. **deliberate, but not concealed** – if the inaccuracy is deliberate, but the person does not make arrangements to hide it

4. **deliberate and concealed** – if the inaccuracy is deliberate, and the person makes arrangements to hide it.

*CH420200*

You must look at all aspects of your case. Deciding on behaviour is not about simply applying tests, but includes thinking about the customer and their situation.

A person may have a learning difficulty, be physically disabled or have caring responsibilities. Such circumstances may drastically interfere with their ability to look after their tax affairs. You must take these on board when establishing behaviour; what is reasonable for one person may not be for someone else.

People do make mistakes. We do not expect perfection. We are simply seeking to establish whether the person has taken the care and attention that could be expected from a reasonable person, taking reasonable care in similar circumstances.

### Intentions of another person (T)

CH81075

For a third-party penalty to apply, another person (T) must intend that the result or outcome of supplying false information (or withholding information) is that the person's (P) document contains an inaccuracy that amounts or leads to

- an understatement of a liability to tax, or
- a false or inflated statement of a loss, or
- a false or inflated claim to repayment of tax.

CH81167 - 68

To establish this you must be able to demonstrate that

- T knew that the information was specifically required to complete a return, and
- T knew that if they gave false information (or withheld information) the return would be wrong, and
- T then gave the false information (or withheld information) knowing that, as a result, that particular return would understate the tax due, or overstate a loss or repayment.

You, therefore, need to establish that T knew the consequences of his or her actions. Not only must T have deliberately chosen to supply false information (or deliberately withhold information), but must have also intended P's return to be inaccurate.

We will now look at these behaviours in more detail, beginning with understanding what is meant by 'reasonable care'.

## 2.2.1 Inaccuracy despite taking reasonable care

CH81130

All customers are required to take reasonable care in their tax affairs. You cannot identify why an error has arisen until you understand the particular customer's abilities or circumstances.

We do not, for example, expect someone who is unrepresented and running a small business, to have the same level of knowledge or expertise as a large multinational company. However, we do expect our customers to demonstrate a greater degree of care over large and complex issues than simple, straightforward ones.

All customers are required to make and keep adequate records to support the entries in their returns. We do not expect all records to be of the same degree of complexity. If a customer has simple tax affairs, then they may only need a simple regime for record keeping, provided they follow it carefully. A customer with larger and more complex tax affairs, will need to put in place more sophisticated systems, and follow them equally carefully.

If someone enters into a transaction or event that they are unfamiliar with, we expect them to find out about the correct tax treatment, including taking advice.

If the customer is still not sure about the tax treatment of an issue, despite taking reasonable steps to establish the correct treatment, then they should tell us about their doubts and draw attention to the details when they submit the return or document. Provided they do this, even if they have arrived at the wrong answer, they have demonstrated that they have taken reasonable care to get the matter right.

CH81130

Even meticulous people can make mistakes. We would accept that inaccuracies occurred despite taking reasonable care if, for example

CH431010

- there was an arithmetical or transposition error that is not so large (either in absolute terms or relative to overall liability for the relevant period), as to produce an obviously odd result, or be picked up by a quality check
- the customer sought our advice, gave the full facts, but we provided incorrect information
- the customer held a different, but reasonable, view of an issue but this was not upheld at a tribunal
- the customer obtained advice from a competent adviser, to whom they gave full facts, but the advice was incorrect.

If a person keeps repeating the same errors, you will have to find out the reason before deciding whether to regard them as made despite taking reasonable care.

You cannot charge a penalty for an inaccuracy that occurred despite taking reasonable care. However, there is one circumstance in which you may treat the behaviour as becoming careless.

CH81080

CH430500

### **Reasonable care can become careless**

CH431020

S3 (2) Sch 24 FA  
2007

If an inaccuracy is made despite taking reasonable care, but then later discovered by the person and they do not take reasonable steps to tell us, we will regard it as being careless. When determining whether reasonable care still applies, you will consider the actions they took, including how promptly they told us about the error after they discovered it.

## 2.2.2 Inaccuracy caused by carelessness

CH81140

CH431010

The term 'failure to take reasonable care' is a parallel to the general law concept of negligence, or failing to take the action that a prudent and reasonable person would do in those circumstances.

When considering whether an inaccuracy has been caused by carelessness, you must be able to identify

- the care that should have been taken
- that there was a failure to take that care
- why it was reasonable to expect the person to have taken the care, taking into account their abilities and circumstances.

A person's intention is not relevant when considering whether they failed to take reasonable care. You are simply deciding whether someone who was taking reasonable care would have made that mistake.

If someone intentionally makes an error, or gives us an inaccurate document, that would be deliberate behaviour.

Examples of some situations that could lead to careless errors are where the customer

- doesn't give enough time to keeping necessary records
- doesn't check the figures
- fails to seek necessary advice
- uncritically accepts advice
- doesn't give an adviser or HMRC the full facts when seeking advice
- fails to check the work done by an adviser as far as they are able
- doesn't take steps to act on the advice given, or to use the records or systems at their disposal
- relies on unreasonable estimates
- relies on uncorroborated statements from third parties.

*CH431030*

Keeping poor quality or inadequate records that lead to an inaccuracy in a return or document, may lead to a penalty. You will have to take a number of factors into account, including whether the level of records kept or standard of record keeping is to be expected for the nature, size and complexity of the business or customer's affairs. You will also need to consider the customer's attitude to record keeping.

You may discover repeated inaccuracies that form part of a behaviour pattern, suggesting a lack of care by the person in developing adequate systems for the recording of transactions or preparing tax returns.

Careless inaccuracies can arise due to the circumstances in a customer's business. In Excise cases, many of the traders' internal management systems are a blend of manual and computer-based systems. The staff may enter duty rate changes or additional lines of product into the stock records, but overlook carrying them forward into the duty accounting systems. Duty rate changes applied to complex accounting systems, such as warehouse stock, can often produce anomalies if all elements of the change are not aligned.

It is, however, important to keep a sense of proportion. Repetition of the same inaccuracy would not always, of itself, indicate a failure to take reasonable care.

**Activity One**

For the purposes of this activity you should ignore any tax implications.

1. Tony has several sales reps, and he decides to provide them with company cars. In view of the number of cars he is buying, he gets a discount of £500 on the forecourt price of each car.

He has to complete a form for each car, which asks for the 'list price' of the car.

The guidance notes accompanying the form do not explain what is meant by 'list price'. However, a telephone helpline number is provided if further assistance is required.

Tony is unsure what is meant by the term 'list price' and decides to telephone the salesman who sold him the cars. The salesman says he doesn't know anything about the form, but 'list price' probably means the price he paid for the car.

Tony decides not to use the telephone helpline number, and simply completes the forms with the price he paid for each car.

Has Tony taken reasonable care when completing the form? Explain your conclusions.

**Activity One (Continued)**

2. Bill, an Excise warehouse manager, is submitting the monthly discrepancy report. This is a spreadsheet showing details of each product line by tax code. Each product line is on a separate line in the spreadsheet, with a 'sum' formula used to total the columns.

Bill's assistant Paul had updated the spreadsheet to include that month's new product lines, but forgot to adjust the 'sum' function to take the new rows into account. This results in an underdeclaration of £15,000.

The report was sent in on time. A compliance check showed that the product line details are correct, with only the tax code totals being wrong.

State whether Bill has taken reasonable care when submitting the report.

**Response**

1. Tony's behaviour suggests a failure to take reasonable care.
  - It is his responsibility to make sure he knows what to put on the form.
  - If he doesn't know, he should try to find out.
  - He has made a limited attempt to find out the answer by telephoning the salesman. However, the salesman has told him he also doesn't know the correct answer.
  - Tony has accepted the advice of someone who was not competent to give him the correct advice. There was a telephone helpline number on the form, but Tony chose not to contact the person who was most likely to be able to answer his query.

2. The inaccuracy is treated as careless.

There is no evidence to suggest that Bill or Paul's behaviour was deliberate.

The actual product line details are correct, according to the internal stock reconciliation, so the requirement of EWER 88 12(6) is met.

**Activity Two**

1. If a person keeps making the same mistake it can **never** be 'despite taking reasonable care'.

|      |                          |       |                          |
|------|--------------------------|-------|--------------------------|
| True | <input type="checkbox"/> | False | <input type="checkbox"/> |
|------|--------------------------|-------|--------------------------|

2. Carelessness is when a customer doesn't bother keeping proper records, and is not then able to make an accurate return.

|      |                          |       |                          |
|------|--------------------------|-------|--------------------------|
| True | <input type="checkbox"/> | False | <input type="checkbox"/> |
|------|--------------------------|-------|--------------------------|

3. Bev works in an outlet shop. She picks up returned designer items cheaply and auctions them on eBay. She doesn't think to declare her profits on her tax return. When she finds out she should do so, she sends an amendment to the return within the 12-month time limit.

Can we consider issuing a penalty for the inaccuracy in the original return?

|     |                          |    |                          |
|-----|--------------------------|----|--------------------------|
| Yes | <input type="checkbox"/> | No | <input type="checkbox"/> |
|-----|--------------------------|----|--------------------------|

**Response**

1. If a person keeps making the same mistake it can **never** be 'despite taking reasonable care'

True

False

You must look at the individual circumstances to find out why the error occurs. It could be, for instance, a one-off slip when inputting data onto the computer for an item that repeats weekly.

2. Carelessness is when a customer doesn't bother keeping proper records, and is not then able to make an accurate return

True

False

Again, you will have to find out all the facts. Provided there is no intent to cause an inaccuracy, circumstances such as these may well be careless.

3. Bev works in an outlet shop. She picks up returned Designer items cheaply and auctions them on eBay. She doesn't think to declare her profits on her tax return. When she finds out she should do so, she sends an amendment to the return within the 12-month time limit.

Can we consider issuing a penalty for the inaccuracy in the original return?

Yes

No

The return contained the inaccuracy. Despite the amendment you would look at the behaviour leading to the omission of the profits. If you concluded it was careless or deliberate, then you would consider issuing a penalty.

### 2.2.3 What is deliberate behaviour?

CH432010

The difference between a deliberate and a careless inaccuracy depends on whether the person intended to include the error or omission in the document, or intentionally submit an incorrect document.

The standard of proof for penalties under Schedule 24 is the civil standard. In deciding whether an inaccuracy was deliberate, you will need to show, based upon available evidence, that it was deliberate based upon the **balance of probabilities**, but for more serious behaviour we would expect stronger evidence. The evidence you gather may be direct or indirect.

CH432020

### Direct evidence

Direct evidence will be rare but could include

- an admission by the person
- written instructions to misrepresent the true position
- an alternative set of records or falsified documents.

CH432030

### Indirect evidence

Indirect evidence is something which indicates that the person knew (or could reasonably be expected to have known) that the document was inaccurate, and you may therefore infer that this was deliberate behaviour.

Examples of indirect evidence that may imply deliberate intention include

- personal involvement – where the inaccuracies are in an area where that person has direct personal involvement, such as drawings or personal bank accounts
- evidence that the person has directly benefited from the inaccuracy (for example, off-record sales used personally)
- scale of inaccuracy – a large error in relation to the overall tax liability is more likely to be noticeable than a small error. When the inaccuracy is substantial compared to the overall tax liability, it is more likely you can infer that the person was aware of it before the document was submitted.

## 2.2.4 Deliberate but not concealed

CH81150

When a person gives us a document that they know contains an inaccuracy, this is deliberate.

**(This text has been withheld because of exemptions in the Freedom of Information Act 2000).**

You must not discuss penalties with a person, or their agent, if you think there is any chance that criminal investigation is appropriate.

CH402160

If a serious matter arises without warning, during a visit or meeting, and you have any doubts as to whether you should proceed, you must withdraw from the meeting and consult your manager.

CH432000

Examples of deliberate inaccuracies in documents might include, knowingly

- systematically paying wages without accounting for Pay As You Earn (PAYE) or National Insurance Contributions (NIC)
- failing to record all sales
- deliberately describing transactions inaccurately, or in a way likely to mislead
- giving a Value Added Tax (VAT) return to HMRC that includes a figure of net VAT due that is too low, because they didn't have the funds to pay the full tax due at that time
- claiming a deduction for personal expenses of such a size or frequency that the inaccuracy **must** have been known
- withdrawing money for personal use from an incorporated business, and not making any attempt to make sure it is treated correctly for tax purposes
- omitting a known asset from an Inheritance Tax (IHT) account.

**Example**

Fiona is the personal representative of her late father's estate. Her father owned a house but Fiona makes no attempt to establish its market value. She includes an estimated value in the IHT account, based on what her father paid for the house many years earlier, although she knows it is worth much more. Fiona has deliberately included a value that she knows to be incorrect in the IHT account. However, she has not taken other steps to conceal the undervaluation.

**Activity Three**

Delroy submitted an IHT account for his late father's estate. The estate exceeds the amount of the IHT 'nil rate band' and is wholly non-exempt. It consists of his late father's own property and a qualifying interest-in-possession in a settlement.

Delroy approached the trustees of the settlement for information for the IHT account, because he did not have access to the settlement's books and accounts. The trustees deliberately did not tell him about a bank account containing £50,000. They

- knew that Delroy needed the information to complete the IHT account
- knew that if they withheld details of the bank account, the IHT account would be wrong, and
- knew that not including the bank account would understate the IHT due.

Delroy submits the IHT account on the basis of the information he was given by the Trustees. Some time later HMRC discovers the understatement.

Describe the behaviour of Delroy and the trustees, and state who is liable for what penalty.

**Response**

Delroy took reasonable care, to the best of his ability, to check that the information given to him by the trustees was accurate and complete, because it was not possible for him to independently check whether the details the trustees gave him were correct.

The trustees deliberately supplied incorrect/incomplete information, knowing that it would make a return incorrect.

The trustees will be liable to a third-party penalty.

Delroy will not be liable to any penalty.

Had it been that Delroy had also failed to take reasonable care, then he may also have been liable to a penalty for the incorrect IHT.

## 2.2.5 Deliberate and concealed

CH81160

CH432020

This is the most serious type of behaviour. The person has not only knowingly and intentionally made errors, but has also taken steps to cover their tracks.

Actions to conceal the errors could be

- creating false invoices to support inaccurate figures in the return
- backdating or postdating contracts or invoices
- creating false minutes of meetings, or minutes of fictitious meetings
- destroying books and records
- systematically diverting takings into undisclosed bank accounts, and covering the traces
- invoice routing, for example, the purported sale or purchase of goods through a tax haven company
- creating sales records that deliberately understate the value of the goods sold; the balance of the full price being paid separately to the person
- describing expenditure in the business records in such a way as to make it appear to be business related when it is, in fact, private
- altering genuine purchase invoices to inflate their value
- compiling false business accounts to support the availability of agricultural or business relief from IHT
- mis-declaring the strength of alcoholic products on paperwork and accompanying documentation.

**Example 1**

George Landry is the director (and 100 per cent shareholder) of Acme Engineering (Shelf 99) Ltd. He has a salary taxed under PAYE each month, plus dividends from his company. In addition to these payments, he draws a further £2,000 every month.

He wishes to avoid showing his director's current account as overdrawn, as he would incur a personal tax bill for a beneficial loan (Section 175 ITEPA), and the company would incur a tax charge under Section 419 ICTA 1988 (loans to participators). He, therefore, creates false purchase invoices to the value of £2,000 per month (including VAT). He records the inflated purchase figure in the business records, and claims input VAT to which the company is not entitled on the quarterly VAT returns.

The extra purchase costs reduce the profits in his accounts, so that the company tax return is also incorrect.

**Example 2**

Delta Fridges PLC buys refrigerators from China and sells them to electrical retail outlets in the UK. The directors set up a company registered in Panama. While the goods continue to be shipped directly from China to the UK, they arrange for paperwork to be produced showing the Panamanian company as an intermediary, with a 10 per cent management fee being charged to the UK company.

This 10 per cent fee is then deposited into offshore personal bank accounts of the directors, and is used to fund loan payments for the purchase of holiday homes they each have in Dubai.

To sum up, you will gather and assess the available evidence and from this draw your conclusion about which of the four error types will apply.

| Error Type                     |  |
|--------------------------------|--|
| Despite taking reasonable care | The customer tried to get it right and took all reasonable steps to make sure that they did so   |
| Careless                       | Parallel with negligent. The customer didn't take the care they should but there was no intent to be inaccurate,<br><br>or<br><br>inaccuracy despite reasonable care that they discovered but took no timely steps to tell us so |
| Deliberate                     | Knowingly getting it wrong and not correcting it   |
| Deliberate and concealed       | Knowingly getting it wrong, not correcting it and taking steps to hide it  |

Now try the following activities to identify the behaviours which gave rise to the inaccuracy.

**Activity Four**

Consider into which behaviour types the following might fall.

1. Mark is a builder. His firm is constructing a housing development. He is also renovating a large stone barn which will become his family home. Most of the purchases for the development come from Sharon's building supplies. She is an old friend. At his request, she agrees to put the address of the development on the invoices relating to the barn. He includes all the barn construction and renovation costs in his books, and assures his accountant that he never puts any personal costs through the business. The accountant, therefore, makes no adjustment for private use.

- Mark's behaviour is

2. Dan pays his employees a Christmas bonus in cash. He knows that he should deduct PAYE and NIC, but chooses not to do so.

- Dan's behaviour is

3. Herbert is an 80-year-old former railway worker. He has cataracts and is in the early stage of Alzheimer's disease. When he fills in his tax return he forgets about his British Railway pension, making no reference to it on the form. He has always shown it in previous years.

- Herbert's behaviour is

**Activity Four (Continued)**

4. Talal keeps accurate business records. Because of cash flow problems, he decides to enter an inflated figure of input tax on one of his VAT returns to reduce his net liability. He discloses the error to HMRC several months later when his cash flow has improved.

- Talal's behaviour is

5. Jane is a self-employed taxi driver. She does not record each fare, and does not always count the cash on hand at the end of her shift; nor does she always retain receipts for her expenditure. Every few days, she attempts to calculate her takings since she last recorded them. Because she has not kept a daily record of income, she has to try to recall approximately how much she took and how much she has spent. At the end of the year she presents her accountant with a box of expenses receipts and a takings book in which she has recorded her takings. The agent prepares the tax return and business accounts from this information.

- Jane's behaviour is

**Activity Four (Continued)**

6. Faruq is a director and shareholder of a company. He has been paid a substantial dividend. When completing his Self Assessment (SA) return he realises that this dividend will result in him being liable to income tax at higher rate (40 per cent). He takes the decision to leave the dividends off his return, and hopes that HMRC will accept the return without checking it.

- Faruq's behaviour is

7. Colin is a plastic surgeon who is employed by his local NHS trust. In addition to his employment, he operates a private patients' clinic at a private hospital nearby. He records only 50 per cent of his private clinic income, and produces invoices showing a reduced amount as having been charged to his patients. He arranges for the other 50 per cent to be paid into an offshore bank account.

- Colin's behaviour is

**Activity Four (Continued)**

8. The stockbroking arm of a large bank undertakes approximately 150,000 transactions each year. A team from Stamp Duty Reserve Tax (SDRT) perform a compliance check.

They find that there is a large number of third-party purchases on behalf of obscure charity clients, and question these.

The Unit Trust Manager, Peter Barnes, is dismissive about the compliance check, slow at responding to correspondence, and provides inadequate details. He insists that there are no errors.

Following copious correspondence and many delays, the compliance officer finally has evidence suggesting that many of the transactions put through as 'charity' purchases were payments to favoured operational staff members of the trust. Faced with the evidence, Peter finally admits to the practice, and that it has been going on for 3 years.

The shortfall of SDRT is £125,000 a year, unaccounted for by the trust. The Unit Trust sack Peter, but they contest the extent of their corporate liability.

- The Unit Trust's behaviour is

**Response**

1. Mark's behaviour is deliberate and concealed. He knows that what he is doing is wrong, and he has taken active steps to hide it by arranging for inaccurate paperwork to be created.
2. Dan's behaviour is deliberate but not concealed. He knows what he should do, but makes the decision not to account for PAYE/NIC in respect of the bonus payments.
3. Herbert's error is likely to be treated as despite taking reasonable care. You would offer him help for the future, possibly finding out whether anyone could act as his representative.
4. Talal's behaviour is deliberate. He knew the correct amount of input tax, and decided to include an inflated figure on the return. The Error Correction Scheme for VAT does not allow for deliberate errors to be corrected in a later return.
5. Jane is disorganised. She cannot be sure that she has returned the correct amount of her profit. Her attitude towards her record keeping amounts to a lack of reasonable care, or **careless**. If the pattern and size of understatement were such that she must have known she was not declaring her full profits, then her inaccuracy would be **deliberate**.

**Response (Continued)**

6. Faruq knows what he is doing, but apart from leaving the dividends off his return makes no attempt to hide them. His behaviour is **deliberate, but not concealed**.
  
7. Colin has also taken steps to conceal a substantial amount of his taxable income by producing incorrect invoices, and by depositing the omitted income into an offshore bank account. His behaviour is both **deliberate and concealed**.
  
8. Peter acted on behalf of the Unit Trust. His behaviour was **deliberate and concealed**. A case of this kind is extreme and may be considered for prosecution.

## 2.3 Gathering Evidence about Behaviour

*CH430000*

It is up to you as caseworker to decide which behaviour type each inaccuracy reflects. You will need to produce an audit trail from the obtaining of facts, up to your decision. It must show why you think that the facts and explanations given to you led you to that particular decision.

*CH433500*

You must obtain approval to your views, before discussing the matter with the customer or their representative. The approval process is covered in Chapter 5.

The records of your evidence will have to be examined by the authorising officer when giving approval to your decision on the behaviour type. They will also have to be produced if the customer appeals against the decision.

For this reason, you must keep records of these facts and any discussions which took place. These will include details of what the customer said and did.

*CH81167*

If an inaccuracy is attributable to another person, you will need to carefully examine the underlying actions that led to the inaccuracy and record your findings.

Although not conclusive, evidence that another person (T) has benefited financially as a result of the inaccuracy in this person (P)'s return or other document may be an important part of evidence of T's deliberate intent.

Evidence may include

- material generated from the compliance visit
- statements made by the customer or their representative
- notes of discussions with the customer
- copies of relevant documentation
- the effect of the inaccuracy on their personal life, such as unexplained availability of cash
- the frequency of the errors - the more often an error occurs the more likely it is to be spotted
- multiple errors - the more that are discovered, the less likely they are to be accidental
- size - a large error will have more of an effect on other transactions or balances, and should be more easily identified by the customer
- significance - if a transaction is particularly important to a person, they are far more likely to notice the effect of any mistakes.

### **Example**

When completing a quarterly VAT return, Sandra makes a transposition error. Input VAT is £1,575,000. She puts £1,755,000. Normally, the trading pattern does not widely fluctuate, but this quarter the VAT payable to HMRC is significantly lower. Any business that has an appropriate system of checks and reviews should notice the changes in expected VAT liability, as well as additional funds. They business should investigate the reasons behind the changes.

### 2.3.1 Previous compliance history

CH420900

You must not take reports from previous compliance checks as evidence about the behaviour leading to the current inaccuracy. This applies even if the customer has been given advice about errors on previous occasions, yet repeats them. Each inaccuracy has to be judged in isolation. Using former errors as evidence to judge current ones is predetermining the outcome.

You may look at any previous compliance history in only two circumstances

- where you and your manager are in doubt as to the **balance of probabilities** in support of the decision
- only when there is real doubt, and only to support a decision of a less serious behaviour category.

You are most likely to look at this when you have a doubt as to whether the customer has taken reasonable care. If records show that they have an exemplary compliance history, this may point to a balance of probabilities that they took reasonable care in relation to the current inaccuracy.

Weigh any explanations offered and be critical, but also try to keep an open mind.

In a meeting, if the person wants to call in their agent for support, you should arrange a further appointment. The agent may be able to give you useful information about the reasons behind the error, but the discussion cannot be delegated to them completely. A return or document is the responsibility of

- the person who signs it (for direct tax purposes)
- the registered entity responsible for making the declaration (for VAT purposes),

so it is their behaviour you are trying to establish, and only they can know all the facts.

CH434000

CH451500

You cannot 'establish' a behaviour type by simply deciding or asserting it. You should try to reach agreement with the customer and have them acknowledge their behaviour. Whether you seek agreement before or after calculating the penalty will be for you to decide, depending upon the individual customer. In many cases, the customer will want to know whether a penalty is due, and the amount, at the same time.

If you cannot reach agreement, then you will have to make a decision on the behaviour. The customer has a right of appeal against your decision. Appeals are covered in Chapter 7.

### 2.3.2 Standard of proof

*CH81190*

*CH420500*

Your standard of proof for both careless and deliberate behaviour is 'balance of probabilities'. This is whether the evidence you have gathered shows that 'under the circumstances' it is more probable than not that the inaccuracy was made carelessly or deliberately. For more serious behaviour, the strength of your evidence will need to be higher than for, say, careless errors.

A deliberate inaccuracy will almost always be dishonest or fraudulent. To meet the 'balance of probabilities' test, the evidence required to establish an inaccuracy as deliberate will have to be particularly strong. This is because the courts have held that there is an inherent likelihood that any given person is honest. Evidence of dishonesty in other matters, such as other tax obligations, may therefore be relevant. If you can show that a person is dishonest in one aspect of their life, it is more likely that they have been dishonest in another.

*See CH82180,  
CH82200, CH82210  
and CH82250*

Your decision about the behaviour is crucial to the overall penalty level. If you have any doubts about your conclusion, you must discuss your findings with your manager/team leader. Do not leave it to the point where penalties have to be authorised.

If you feel that there may be a more serious behaviour than you have established, but cannot see how you can demonstrate it, you should discuss this with your manager. Ensure that your reasons and the manager's input (including any additional action to be taken) are recorded in the papers/on Electronic Folder (EF).

You will usually treat each inaccuracy individually, as each could be caused by different behaviour and be subject to a different penalty. Someone who has deliberately created and concealed an irregularity can still make careless errors as well.

*See CH82200*

Inaccuracies which are broadly similar can sometimes be grouped together for calculating the penalty, provided the customer or their agent agrees. This is covered further in Chapter 4.

If the person chooses not to co-operate following Human Rights Act (HRA) advice, then the meeting or visit should be terminated, and evidence will have to be obtained by correspondence, using formal powers. When you have gathered all the information and documents to settle the tax liability, you can come to a decision regarding the behaviour and disclosure for penalty purposes.

**Activity Five**

You are in an interview with a customer and have identified inaccuracies. What questions might you ask to help you decide on the behaviour type?

**Response**

Your questions might include

- In this business, who is responsible for what?
- What is your role?
- Has the business, its personnel or anything else changed from earlier years?
- What information did you give to your agent?
- If the return was prepared by your agent, did you check the figures the agent entered. If so, how did you check?
- Did you review the whole of the return before you signed?
- What steps did you take to try to make sure the document was correct?
- What documentation do you have that can support your conclusions?
- What is the extent of the problem? Has it ever happened before?
- Does the problem affect earlier years?
- If you did not know what you should include, what advice was available to you? What advice did you ask for and from whom?
- If you were unsure why didn't you seek advice?

### 2.3.3 Speaking to third parties

CH420700

On a visit to business premises, the customer may agree to you speaking to a third party, such as a bookkeeper or wages clerk, to gather evidence or understand behaviour. You must not discuss the imposition of penalties with the third party.

Their evidence can be crucial to understanding the business, but this is a sensitive area. Company officers or business owners may be happy to delegate a VAT or employer compliance visit or a Corporation Tax (CT) or Income Tax (IT) records examination to an employee. They may be less happy if that visit results in a penalty.

Consider carefully any questions to employees, and restrict them to establishing the facts about what went wrong, and what part they took. You may place an employee in a difficult position by asking questions about matters beyond their immediate knowledge and responsibility. You should not put them under any pressure to speak about matters outside their duties. If you need to speak the owner/director and that person is not available, you will have to arrange a further meeting.

If the employer asks you not to speak to the employees, then you should make no further contact.

In status cases, however, when you are trying to establish whether workers are employees or self-employed, you will have to have meetings with workers with or without the engager's agreement. If the engager agrees you can interview the workers on the premises.

## 2.4 Correcting Errors

### 2.4.1 Indirect taxes

There are several indirect taxes error-correction regimes which allow

CH81141

- errors made despite taking reasonable care

VAEC7120

and

- careless errors

in previously submitted returns to be adjusted.

The adjustment is made in the return for the period in which the errors are discovered, provided it is within certain monetary limits. The customer should make a note of the error in his or her tax or duty account, including when it was discovered.

CH81142

The VAT error correction limits, below which errors can be adjusted in the return for the period of discovery, are given below. These limits apply to errors discovered in accounting periods beginning on or after 1 July 2008. The monetary limits for other indirect taxes are set out in CH81142.

#### VAT

VAEC7180

The net value of the error must not exceed the greater of

- £10,000, or
- 1 per cent of the box 6 figure on the VAT return, for the period of discovery, subject to an upper limit of £50,000.

VAEC7120

If the errors cannot be adjusted in the return for the period of discovery, the person

- must notify HMRC of the errors in writing, either by using form VAT652 or by letter

and

- must not make an adjustment for the errors on a later return.

If a trader makes an inaccuracy despite taking reasonable care, **and** the net value is below the threshold, then we shall regard the error correction as 'taking reasonable steps' to inform us of the inaccuracy.

VAE7140

It is important to note that despite the error-correction regime described above, if a customer has made a careless error, then for the purpose of Schedule 24, they have **not** made a disclosure simply by correcting the mistake. We may still issue a penalty for inaccuracies in the earlier return(s) that led to the adjustments.

Therefore, at the time of making the error correction, the customer will have to consider whether they regard the error as despite taking reasonable care or careless, and whether to make a separate disclosure of the details.

## 2.4.2 Direct taxes

Similarly, a customer who is within SA or CTSA has 12 months from the filing date of their return in which they can amend the original return. If we enquire into the return, we must look at the behaviour behind any inaccuracies in the original return, before deciding whether a penalty applies.

Petroleum revenue tax is not given a 12-month amendment window in its statute. Once the return is received, any inaccuracy will be considered for a penalty depending on the underlying behaviour that caused it.

## Review

This chapter started at the point in a compliance check when you have identified either an inaccuracy in a document, or a failure to notify an under-assessment.

For an inaccuracy, you need to determine the behaviour that led to it. You do not need to determine behaviour for under-assessments.

If an inaccuracy is caused by the deliberate actions of a third party with the intent that a return or document should be inaccurate, a penalty may be charged on the third party.

Four types of behaviour were explained and described

- reasonable care
- careless
- deliberate, not concealed
- deliberate with concealment.

We looked at the meaning of each behaviour.

- Reasonable care includes or means keeping adequate records appropriate to the financial activity and taking advice when warranted. We cannot charge penalties where reasonable care has been taken.
- A careless inaccuracy will be one that would not be made by a person taking reasonable care. Careless equates to the legal concept of negligence.
- Deliberate and not concealed is the behaviour from a person who knows they are submitting an inaccurate document, and take no particular steps to hide it.
- Deliberate and concealed is the most serious behaviour type. This involves knowing that there is an inaccuracy but taking conscious action to try to hide the inaccuracy.

**(This text has been withheld because of exemptions in the Freedom of Information Act 2000).**

Invite and welcome the customer's help with your enquiries, but make them aware that they do not have to co-operate. Explain the consequences if they choose not to, including that you may need to use information and inspection powers in Schedule 36 FA 2008.

We explored the kinds of evidence you will need to gather about the behaviour that led to the inaccuracy.

We looked at the importance of recording your findings and notes of meetings or discussions, as they will support your decision to the authorising officer, and possibly be cited in a tribunal hearing.

Finally, we explained how you should assess the evidence to come to a reasonable conclusion about behaviour. This will take into account the actions and intention of the customer and also their personal circumstances and areas of expertise.

In Chapter 3, Disclosing Inaccuracies, we will look at how you decide whether a disclosure is unprompted or not, and what steps the customer can take to reduce their penalty.

### Learning Check

1. State the four behaviour types.



- 
- 
- 

2. You cannot charge a penalty if the inaccuracy arose

|          |                                     |                          |
|----------|-------------------------------------|--------------------------|
| <b>a</b> | because of deliberate behaviour     | <input type="checkbox"/> |
| <b>b</b> | despite taking reasonable care      | <input type="checkbox"/> |
| <b>c</b> | for failing to take reasonable care | <input type="checkbox"/> |

3. When a return is incorrect because of the actions of a third party, what are the significant elements to consider for a penalty?

That the third party

- a. supplied incorrect/withheld information
- b. carelessly supplied incorrect/withheld information without checking whether it would make a return incorrect
- c. deliberately supplied incorrect/withheld information intending that it should make the return incorrect
- d. deliberately supplied incorrect/withheld information without checking whether it would make a return incorrect.

4. Give three examples of 'reasonable care'.

- 
- 
- 

5. When deciding on a person's behaviour you will

|          |   |                          |
|----------|---|--------------------------|
| <b>a</b> | treat everyone the same   | <input type="checkbox"/> |
| <b>b</b> | look at the person's circumstances  | <input type="checkbox"/> |
| <b>c</b> | record only matters where the customer disagrees with your conclusions, in case it goes to tribunal | <input type="checkbox"/> |
| <b>d</b> | record only what you agree upon because it won't go to tribunal                                     | <input type="checkbox"/> |

## Learning Check – Answers

1. State the four behaviour types.

- Reasonable care
- Careless
- Deliberate but not concealed
- Deliberate and concealed.

We looked at the behaviour types in sub-chapter 2.2

2. You cannot charge a penalty if the inaccuracy arose

|          |                                     |                                     |
|----------|-------------------------------------|-------------------------------------|
| <b>a</b> | because of deliberate behaviour     | <input type="checkbox"/>            |
| <b>b</b> | despite taking reasonable care      | <input checked="" type="checkbox"/> |
| <b>c</b> | for failing to take reasonable care | <input type="checkbox"/>            |

This is covered in sub-chapter 2.2.1

3. When a return is incorrect because of the actions of a third party, what are the significant elements to consider for a penalty?

That the third party

- c. deliberately supplied incorrect/withheld information, intending that it should make the return incorrect

You looked at this in sub-chapter 2.2

4. Give three examples of 'reasonable care'.
- Setting up records or systems appropriate to the activity, and carefully maintaining them.
  - Finding out about unfamiliar subjects, including taking advice.
  - If still unsure, drawing attention to doubts when submitting the return or other document.

Reasonable care is described in sub-chapter 2.2.1

5. When deciding on a person's behaviour you will

|          |   |                                     |
|----------|---|-------------------------------------|
| <b>a</b> | treat everyone the same   | <input type="checkbox"/>            |
| <b>b</b> | look at the person's circumstances  | <input checked="" type="checkbox"/> |
| <b>c</b> | record only matters where the customer disagrees with your conclusions, in case it goes to tribunal | <input type="checkbox"/>            |
| <b>d</b> | record only what you agree upon, because it won't go to tribunal                                    | <input type="checkbox"/>            |

Gathering details on behaviours is in sub-chapter 2.3

Customer focus is at the heart of our work on penalties for inaccuracies. When establishing behaviour, it is vital that you consider the person's circumstances and how they affected behaviour. Whatever your initial views, it is important to record all the evidence you gather, so that, no matter how the enquiry develops, you can demonstrate that you have made a reasonable decision.

## Before Moving On

If you have successfully completed the learning check, you will have achieved the study objectives, which are to

- state the four types of behaviour that lead to inaccuracies.
- state for which behaviour types you may issue a penalty
- describe when you would consider a third party penalty
- provide three examples of reasonable care
- state why you need to keep evidence about the inaccuracies and customer behaviour.

If you have not met any of the objectives, go back and reread the relevant part(s) of the chapter before moving on. If you are still having problems, make a note of them for discussion with your manager.