
HMRC REVIEW OF POWERS, DETERRENTS AND SAFEGUARDS: PENALTIES FOR INCORRECT RETURNS & FAILURE TO NOTIFY A TAXABLE ACTIVITY

Who is likely to be affected?

1. Individuals and businesses who understate their tax liability, deliberately or by failing to take reasonable care in completing returns for:
 - environmental taxes (aggregates levy, climate change levy, landfill tax);
 - excise duties (alcohols, tobacco, oils, gambling and air passenger duty);
 - stamp duties (stamp duty land tax, stamp duty reserve tax);
 - accounting for recovery of student loans by employers; and
 - inheritance tax, insurance premium tax, pension schemes and petroleum revenue tax.
2. Individuals and businesses who fail to notify HM Revenue & Customs (HMRC) of a new taxable activity by the required date, where there is tax and / or National Insurance Contributions (NICs) unpaid as a result.
3. This measure will not have effect for tax credits.

General description of the measure

4. Legislation will be introduced in Finance Bill 2008 to extend the provisions enacted in Schedule 24 to the Finance Act (FA) 2007, to create a single penalty regime for incorrect returns across all the taxes, levies and duties administered by HMRC. The penalty will be determined by the amount of tax understated, the nature of the behaviour giving rise to the understatement and the extent of disclosure by the taxpayer. The use of suspended penalties will be extended.
5. Provision will also be made to extend and adapt Schedule 24 to FA 2007 to cover penalties for failing to register or notify HMRC of a new taxable activity across all the taxes, levies and duties administered by HMRC, including late VAT registration.

Operative date

6. The new provisions will have effect from a date to be appointed by Treasury Order. For incorrect returns, this is expected to be for return periods commencing on or after 1 April 2009 where the return is due to be filed on or after 1 April 2010. New penalties for failure to notify are expected to have effect for failure to meet notification obligations that arise on or after 1 April 2009.

Current law and proposed revisions

7. The measure will repeal a large number of different penalty provisions which are specific to each of the taxes, levies or duties covered and replace these with a single legislative framework for penalties for incorrect returns and another similar one for failing to notify a taxable activity by the required date.
8. The new provisions for incorrect returns will provide for penalties in line with Schedule 24 to FA 2007, which are based on the amount of tax understated, the nature of the behaviour and the extent of disclosure by the taxpayer. There will be no penalty where a taxpayer makes a mistake but there will be a penalty of up to:
 - 30 per cent for failure to take reasonable care;
 - 70 per cent for a deliberate understatement; and,
 - 100 per cent for a deliberate understatement with concealment.
9. The measure will provide for each penalty to be substantially reduced where the taxpayer makes a disclosure (takes active steps to put right the problem), more so if this is unprompted. For an unprompted disclosure of a failure to take reasonable care the penalty could be reduced to nil. Where a taxpayer discloses fully when prompted by a challenge from HMRC, each penalty could be reduced by up to a half.
10. Where a return is incorrect because a third party has deliberately provided false information or deliberately withheld information from the taxpayer, with the intention of causing an understatement of tax due, there will be a new provision allowing a penalty to be charged on the third party.
11. The measure will also provide for reformed penalties for some specific excise duty wrongdoings: misusing goods subject to reduced excise duty rates, e.g. red diesel; and, handling goods on which excise duty should have been paid but has not.
12. For failure to notify a taxable activity there will be no penalty unless there is tax and / or NICs due but unpaid as a result, nor where the taxpayer has a reasonable excuse for the failure. Otherwise there will be a penalty of:
 - 30 per cent of tax unpaid for non-deliberate failure to notify;
 - 70 per cent of tax unpaid for a deliberate failure to notify; and
 - 100 per cent of tax unpaid for a deliberate failure with concealment.Each penalty will be substantially reduced where the taxpayer makes a disclosure (takes active steps to put right the problem), more so if this is unprompted.

13. For Class 2 NICs, the provisions will replace the fixed penalty of £100 for notification more than three months after starting self-employment with a behaviour based penalty. The obligation to notify remains unchanged.
14. The measure will include full and explicit provisions for the right of appeal against all penalty decisions.
15. HMRC will continue to consult on guidance on the operation of these penalty provisions between the date the Finance Bill 2008 receives Royal Assent and the implementation of the changes. It is intended that guidance will be published well ahead of implementation.
16. This measure was the subject of a consultation document published on 10 January 2008 – *Penalties Reform: The Next Stage with draft clauses and explanatory notes*. A summary of responses to that consultation and a Final Impact Assessment, including an explanation of any resulting changes, will be published shortly.

Further advice

17. If you have any questions about this change, please send an email to powers.review-of-hmrc@hmrc.gsi.gov.uk or contact Maria Richards on 020 7147 3223. Information about Budget measures is available on the HM Revenue & Customs website at www.hmrc.gov.uk