

# **Self Assessment: the legal framework**

**A guide for Inland Revenue  
Officers and Tax Practitioners**

*Notes on the new 'process now - check later' system for  
the assessment and collection of tax*

# Statutory References

The legislation dealt with in this guide is contained in Sections 178 to 199 and Schedule 19 of the Finance Act ('FA') 1994, and in Sections 103 to 116 and Schedule 20 and 21 of the Finance Act ('FA') 1995.

Unless otherwise stated all statutory references in this guide are references to the 'Taxes Management Act ('TMA') 1970' as amended by either FA 1994 or FA 1995. References to TMA 1970 are further distinguished using **bold print** and *italics* as follows:

Section 8 TMA 1970 refers to that Act **prior to** amendment by either FA 1994 or FA 1995;

**Section 8** refers to that Act **as amended** by either FA 1994 or FA 1995.

References to the original or amended sections of both the 'Income and Corporation Taxes Act ('ICTA') 1988', and the 'Capital Allowances Act ('CAA') 1990' are distinguished using **bold print** and *italics* in the same way.

## Meaning of 'business'

Unless otherwise stated the term 'business' is used in this guide in place of the statutory terms 'trade, profession or vocation'.

## Meaning of 'profits'

Unless otherwise stated the term 'profits' is used in this guide in place of the statutory income tax terms 'profits or gains', 'income' and 'profits, income or gains'.

## Meaning of 'tax year'

The term 'tax year' is used in this guide in place of the statutory term 'year of assessment' and is the 12 month period from 6 April to the following 5 April.

## Meaning of 'Officer of the Board'

The term 'Officer of the Board' is used in the new legislation in place of the more traditional terms 'Inspector' and 'Collector'. This is because the introduction of Self Assessment coincides with a change programme within the Inland Revenue that includes a very extensive internal reorganisation. New ways of working will mean that people in the Revenue will not be restricted to working within the old specialisms. But the officers of the Board who perform the work will be of similar rank and training to those who perform analogous tasks today.

## Period covered by tax return

Under the existing legislation the tax return for '1994/95' requires a return of income for the year ended 5 April 1994 and a claim to allowances and reliefs for the year ended 5 April 1995.

Under Self Assessment a tax return will require the return of income, and any claims, to be **for the same period**. So throughout this guide references to tax returns in the form '1997/98' indicate returns of both income and claims for the year ended 5 April 1998.

# Foreword

i) The Finance Act 1994 contained the main legislation for a major reform of the tax system known as '**Self Assessment**'. This reform will introduce a fairer and more straightforward system for people who receive tax returns. Specifically it will

- simplify the procedure for making tax returns and paying tax
- simplify the rules for working out an individual's annual income tax bill
- give taxpayers greater control of their own tax affairs, including the option to calculate their own tax liability (to 'self-assess').

ii) The key change is that it will be taxpayers who create the legal charge to tax by making a '**self-assessment**' of their tax liability for any year. These self-assessments will replace the Revenue assessments issued under the current system.

A taxpayer will be able to make a self-assessment by either

- including a calculation of tax liability in his or her tax return, or
- filing the tax return only, so that the Revenue can do the calculation, and advise the taxpayer of the tax to pay.

Either way, where the information in the return is complete and correct the taxpayer will simply have to pay the tax calculated to be due.

iii) The Finance Act 1995 contains further legislation for Self Assessment. The topics dealt with include

- rules to bring the taxation of employees within the new Self Assessment regime;
- rules to bring the taxation of non-residents within the new Self Assessment regime, including non-resident landlords.

iv) The original version of this book was published in 1994 as the second in a series of guides on Self Assessment for tax practitioners - including accountants and solicitors - and the Inland Revenue's own staff.

Self Assessment is a very large reform and an important step towards simplification of the tax system. The Inland Revenue recognises the importance of providing clear guidance on the new rules, to explain the new system and ensure that everyone affected understands their role, so that they can comply with their new obligations.

This book deals with the changes to the administration of direct taxation that will apply in the Self Assessment regime. It is issued as part of our commitment to working in partnership with practitioners to ease the way for all concerned in the introduction of Self Assessment.

This guide has now been updated to include the computational aspects of Self Assessment dealt with in the Finance Act 1995. This material forms the basis of two new chapters: 'Claims, elections and notices' (Chapter 6); 'Self Assessment for non-residents' (Chapter 7). The Finance Act 1995 also contains some amendments and additions to the FA 1994 material. These have been incorporated in the appropriate sections of the original chapters, together with some additional guidance on points which seem to be causing particular difficulty.

Except where the new material forms the basis of a new chapter it is identified by back shading.

**To avoid confusion copies of the original version of this guide should be destroyed.**

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# 1 Self Assessment: an overview

*Self Assessment: a completely new approach to the assessment and collection of tax*

- 1.1 Changes announced by the Chancellor of the Exchequer in March 1993 heralded the introduction of the most fundamental reform of the direct tax system since the introduction of PAYE. Legislation to pave the way for these changes was included in the 1994 Finance Act.
- 1.2 This book deals with changes to the system for the assessment and collection of tax. The changes are designed to make the system more efficient for all concerned - taxpayers, practitioners and the Revenue - and more straightforward, clearer and fairer for taxpayers and practitioners.
- 1.3 Self Assessment affects individuals who receive returns together with partnerships and companies. For individuals and partnerships the first year to which the changes described in this book will apply is 1996/97 (although for some partnerships the rules will not apply in full until 1997/98). For companies the changes will apply for accounting periods ending on or after an 'appointed day' that will not be earlier than 1 April 1996. Most of the changes relating to individuals also apply to trustees.
- 1.4 Self Assessment is central to the Change Programme of the Inland Revenue. This Programme, which runs over the 10 years to 2002, will enable the Revenue to adapt to modern day requirements, and to meet the objectives of the Government and the needs of the Revenue's customers. It involves a re-organisation of its office structure, notably bringing together assessment and collection functions, greater use of information technology, changes in the way the Revenue manages its work and people, and simplification and streamlining of its procedures.
- 1.5 The present rules for the assessment and collection of tax are complex and involve considerable duplication of work. Taxpayers are required to supply information to the Revenue so that the Revenue can issue an assessment, the legal charge to tax. In other words the responsibility for getting the tax right is split between the taxpayer and the Revenue. Too often this division of responsibility creates unnecessary problems and conflicts.
- 1.6 In addition there are different rules for different types of income and chargeable gains, including the dates on which the tax is paid. A taxpayer may therefore have more than one assessment for any given period, often dealt with in different Inland Revenue offices.
- 1.7 Self Assessment introduces a requirement to file returns by a fixed date and to pay all income tax (from whatever source) and capital gains tax according to a fixed set of dates. For each tax year an initial payment on account of income tax will be due on the 31 January in that year. A second payment on account will be due on the following 31 July, and a final balancing payment of any residual income tax due, and any capital gains tax, on the 31 January following (which will also be the normal filing date for that year's return).
- 1.8 This will mean that from January 1998 taxpayers will have only one annual tax bill in place of the multiple demands received now. The tax bill will be based on the taxpayer's own calculation of the liability (a self-assessment) which will be required with the return. The Revenue will supply a regular statement of the taxpayer's running account with the Revenue, recording charges and payments received and identifying the key dates for complying with obligations throughout the year.

- 1.9 Although all taxpayers will be required to provide the information on which a self-assessment is based, they will actually have the option of choosing whether to calculate their own liability or leaving it to the Inland Revenue. Customer service will also be enhanced through creation of new tax enquiry centres, the introduction of a system for giving binding post-transaction rulings and the ability to deal with a focal point of contact within the Revenue.
- 1.10 To help those taxpayers who choose to calculate their own tax liability Self Assessment will involve the taxing of business profits and investment income on a current year basis rather than the more complex preceding year basis. And partnership profits will be taxed on the individual partners rather than on the partnership itself.
- 1.11 Self Assessment entails a fundamental change in the way that the Revenue handles returns. Returns will be due by a fixed date each year (normally 31 January) and there will be automatic sanctions for failure to comply with those time limits. The Revenue will in future process payments and returns on receipt as though they were complete but will then have the right to enquire into any return, to check its accuracy, within fixed time limits.
- 1.12 Self Assessment gives taxpayers more control over their own tax affairs. Provided the tax return is complete and correct they will only have to pay the tax they calculate to be due and contact with the Revenue will be reduced to a minimum.
- 1.13 For practitioners the present costly rigmarole of dealing with estimated assessments and appeals will be swept away. In future the assessment will be in the taxpayer's figure, not one provided by the Revenue where the onus is placed on the taxpayer to displace it. This should make for a less confrontational system.
- 1.14 For the Revenue, the introduction of a 'process now - check later' system enables more time proportionately to be spent on its two core activities of customer service and compliance.
- 1.15 This book contains a description of the legal framework for the Self Assessment system as introduced by the 1994 and 1995 Finance Acts. It covers
- the procedures for making personal tax returns, including the self-assessment (Chapter 2)
  - the payment of tax (Chapter 3)
  - formal procedures for Revenue enquiries into the accuracy of returns (Chapter 4)
  - the procedures for making partnership returns and for enquiries into the accuracy of those returns (Chapter 5)
  - Claims, elections and notices (Chapter 6)
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## *Introduction*

- 2.1 Under the existing rules a personal tax return is merely a notice requiring a return of information. The information to be entered in the return is the information that the Revenue requires for 'assessing a person to income tax' (S.8(1) TMA 1970).
- 2.2 S.8(1) TMA 1970 is a perfect example of the way in which the current rules for the assessment and collection of direct taxes divide responsibility between the taxpayer and the Revenue. On the one hand the taxpayer is responsible for providing certain information to the Revenue. But it is the Revenue alone which is responsible for using that information to calculate the tax due, and the Revenue alone which is responsible for creating a legal debt (the assessment) which the taxpayer must pay. If the taxpayer has more than one source of income it is possible that more than one assessment will be required.
- 2.3 Perhaps there was a time when this arrangement worked efficiently. But it is now a cause of frustration for both taxpayers and Revenue alike.
- 2.4 For example conscientious taxpayers may include an accurate computation of the tax due with their tax return. But they have no control over their own tax affairs because they must still rely on the Revenue to generate the correct legal charge. Conversely a less conscientious taxpayer may deny the Revenue the opportunity to generate the correct legal charge until the last possible moment. Such taxpayers tie up resources and increase administration costs.
- 2.5 Self Assessment transfers the responsibility for creating the correct legal charge to the taxpayer. Or to put it another way, Self Assessment allows taxpayers to take control of their own tax affairs, if they choose to do so.
- 2.6 Under Self Assessment a tax return will still be a return of information. But the information required will be all the information needed to calculate the taxpayer's total taxable income (from all sources) and any chargeable gains, for the period covered by the return. The calculation of the tax due may then be carried out by either
  - the taxpayer, whose calculation of the tax due - a 'self-assessment' - will form part of the return, or
  - the Revenue. All such 'Revenue calculations' will subsequently be treated as if they were self-assessments. So these calculations should simply be regarded as assistance provided by the Revenue to help taxpayers self-assess.
- 2.7 There will be fixed filing dates for completed tax returns. The annual filing date for a return issued at the normal time will be the 31 January following the tax year to which the return relates. So, for example, the annual filing date for a return of income for the year ended 5 April 1998 will be 31 January 1999.
- 2.8 Different filing dates will apply where a return is issued late, to allow a reasonable amount of time for the return to be completed. In Revenue calculation cases earlier filing dates will apply, to allow the Revenue to calculate the tax due and notify the taxpayer accordingly.
- 2.9 A legal charge to tax will be created by the submission of a completed self-assessment, or, in Revenue calculation cases, by the issue of the notice of the tax payable. The due date for payment of that tax will be the annual filing date for the tax year to which the completed return relates. This charge will arise automatically, without the need for additional action by the Revenue. So the Self Assessment return will combine the properties of both the current tax return and the current notice of assessment.

2.10 There will be sanctions to deter late filing of returns, including automatic penalties.

2.11 Revenue responsibilities will be clearly focused on the processing of returns and on enquiries into the accuracy of the returns. Initial processing will include the correction ('repair') of any obvious errors in the return that are identified at that stage and, where required, Revenue calculations.

**Time at which the new rules will apply**

***Section 199(2) FA 1994***

2.12 The first of the new returns will be sent out in April 1997 (or earlier) requesting details of income for the year ended 5 April 1997 (or for the period forming the basis of assessment for the tax year 1996/97). These returns will be due back by 30 September 1997 if the taxpayer requires Revenue assistance in calculating the tax due, or by 31 January 1998 if the taxpayer calculates the tax due.

# Personal returns

## *Changes to the rules for the issue and completion of personal tax returns*

**The return will be required to establish a taxpayer's net tax liability on total income and any chargeable gains**

### **Section 8(1), (1A), and (5)**

2.13 Under the new system a tax return will still be a notice issued to the taxpayer by '*an officer of the Board*' requesting a return of information. But this information will be required for '*establishing the amounts in which a person is chargeable to income tax and capital gains tax for a year of assessment*'.

2.14 A single return will cover the taxpayer's 'total income'. This means that a return will be required for all sources of taxable income. And the amounts returned should be the *net* amounts of any such income, after taking into account

- any relief, allowance or repayment for which a claim is made;
- any credit for tax deducted at source (or treated as deducted at source, or treated as paid).

In other words under Self Assessment a return is required to determine **the net income and capital gains tax due for any tax year**.

**There will be fixed time limits for filing a return**

### **Section 8(1)(a) and 8(1A)**

2.15 The time limits for filing a return, complete with a self-assessment, will be fixed as either

- 31 January following the tax year to which the return relates, or
- if the return is issued 'late', that is after 31 October following the tax year to which the return relates, three months from the date of issue of the return.

2.16 Earlier filing dates apply where a Revenue calculation is required (*see para 2.33*). In all cases the time limits will provide a more realistic time scale for completion of the return than the current 30 day time limit. It should also be noted that returns may be filed early, even though payment will not be required until the statutory due date.

**Time at which a return is filed ('delivered')**

2.17 '*Deliver to the officer*' (e.g. **Section 8(1)(a)**) is generally taken to mean that the return is in the hands of the officer '*on or before*' the relevant day. However, as a practical measure, the Inland Revenue will normally accept a return as having been filed on time if it is clear that the taxpayer took steps to ensure that would be the case, although for some reason it was delayed thereafter (for example, by a post office delay).

## **There will be automatic penalties for failure to file a return on time**

### ***Section 93***

- 2.18 If the time limits for the filing of tax returns are not met fixed penalties will automatically arise. In the most serious cases additional daily or tax geared penalties may also be sought (*see paras 2.67 to 2.79*).

## **And the Revenue may make a determination of the tax due**

### ***Section 28C***

- 2.19 Where a taxpayer fails to file a return the Revenue will be able to make a determination estimating the tax due (*see paras 2.80 to 2.88*).

## **The fixed filing dates for returns also define the due dates for the payment of tax**

- 2.20 In most cases the filing dates for returns with completed self-assessments will also be the due dates for the balance of any tax payable for the period covered by the return (*see Chapter 3 for details*).
- 2.21 And in most cases interest will be payable on any unpaid tax from the due date for payment. In addition to any interest there will be an automatic tax geared surcharge for failure to pay the tax due on time which will also attract interest if paid late. But this surcharge will not come into effect until 28 days after the due date for final payment (*see Chapter 3 for details*).

## **Accounts, statements and documents may be required with the return**

### ***Section 8(1)(b)***

- 2.22 The taxpayer may be asked to provide '*accounts, statements or documents*' relating to the information in the return *with the return when it is filed*.

The legislation allows for business accounts to be required with the return. But in practice taxpayers will be asked to enter the relevant accounts information in a special section in the tax return. The inclusion of this 'standardised accounts information' in the return means that separate accounts will not be required unless the business is particularly large or complex. (The accounts should be retained as they may be required in an enquiry into the accuracy of the return.)

- 2.23 The reference to '*documents*' is not a reference to business books and records, or to similar documents. It is simply a reference to any documentary evidence that may be required with the return. For example, if a particular tax credit is to be allowed then evidence of the tax deducted at source may be required, perhaps in the form of share dividend tax credit vouchers or Sub-contractors certificate SC60.
- 2.24 But there will be a new statutory requirement to keep records and the Revenue may ask to see these records if it opens an enquiry into the accuracy of the return. For people in business any records must be kept for 5 years from 31 January following the tax year to which they relate (the annual filing date for that year), or, if later, until the completion of a formal enquiry into the accuracy of the return.

- 2.25 For people not in business the statements and documents on which the return is based must be kept for one year from the end of the annual filing date or, if the return is filed late, for approximately one year from the date on which the return is filed. But in any case in which an enquiry is made into the accuracy of the return the records must be kept at least until that enquiry is complete. (*See paras 2.98 to 2.111 for details of the record keeping obligation and paras 4.42 to 4.70 for details of the rules governing Revenue requests for documents during the course of an enquiry.*)

### **A partner's share of any partnership income must be included in his own tax return**

#### ***Section 8(1B) and 8(1C)***

- 2.26 Under the new rules partners will be individually responsible for the tax due on their share of any partnership profit, whether the profit from a business carried on by the partnership or the income on investments held by the partnership. So the share(s) of partnership profit must be included in each partner's personal return.
- 2.27 Similarly partners will be required to include their share of partnership losses, tax credits or of partnership charges, in their own return.
- 2.28 Although partners will be individually responsible for the tax due on their share of partnership profits all matters relating to the calculation of those profits, and to the allocation of profits between partners, will be dealt with through a partnership return (*see Chapter 5*). So as far as their own returns are concerned each partner will simply be responsible for ensuring that the share of profits shown in their own tax return equals the share allocated to them in the partnership return.

#### ***Self-assessment***

### **All tax returns will include a 'self-assessment' of the tax due**

#### ***Section 9(1)***

- 2.29 Taxpayers will be required to include an assessment in their return showing the tax due for the tax year to which the return relates. This self-assessment will be based on the information contained in the return and will create a legal charge to tax.

The self-assessment should take into account any relief, allowance or repayment of tax for which a claim is made in the return.

Superficially the process of self-assessment is simply a change in the person responsible for calculating the tax due. But the true essence of self-assessment is that the legal charge to tax will no longer depend on an officer of the Board making a judgement on the accuracy of the information contained in a return. This is true whether a taxpayer submits a completed self-assessment, or submits the return early enough for the Revenue to do the calculation (*para 2.32*).

- 2.30 A self-assessment will be required even though the tax due may in fact be 'nil' (for example, in any case in which the taxpayer's total chargeable income for the year is less than the personal allowances due for that year).
- 2.31 Similarly, a self-assessment will be required even though the taxpayer may be entitled to a net repayment of tax (for example, a repayment of tax deducted at source).

**But if the taxpayer files the return early enough the Revenue will assist in the calculation of the tax due**

**Section 9(2)**

- 2.32 The requirement to include the self-assessment with the return will apply to all taxpayers *except* those who submit the information section of the return in sufficient time for the Revenue to calculate the tax due.
- 2.33 The special time limits for filing the information section of the return on its own are:
- 30 September following the tax year to which the return relates
  - where the return is issued after 31 July following the tax year to which the return relates, two months from the date of issue of the return.
- 2.34 It is essential that all taxpayers comply with the filing date rules at **Section 8(1A)** (*para 2.15*) whether they calculate the tax due themselves or whether the calculation is made by the Revenue. This is because those filing dates are directly linked to the due dates for the payment of the tax due.
- 2.35 So the time limits at **Section 9(2)** are set to ensure that any return filed without a tax computation is submitted early enough for the Revenue to
- calculate the tax due and
  - issue a copy of the calculation to the taxpayer before the due date for payment of the tax.
- 2.36 Where, exceptionally, the Revenue fails to notify the taxpayer of the tax due in time for the correct tax to be paid at the due date for payment, even though the taxpayer filed a return within the time limit for Revenue assistance, any interest or surcharge arising in the period of delay attributable to the Revenue will be forgone.

**Filing date for taxpayers whose additional tax liabilities are collected through PAYE**

- 2.37 Taxpayers with Schedule E sources may wish to continue the current practice of having any additional tax liabilities collected through PAYE by a coding adjustment, rather than by direct payment. The Revenue will be encouraging all such taxpayers to file by the earlier return date of 30 September, including those who choose to complete their own self-assessment.

**Revenue calculations**

**Section 9(3)**

- 2.38 Although a taxpayer may specifically request that the Revenue calculate the tax due a formal request is not actually necessary. If a return is filed without a self-assessment, and it is filed within the specified time limits for Revenue calculations, an officer of the Board is automatically required to calculate the tax due using the information in the return and to issue a copy of the calculation to the taxpayer.

The process of Revenue calculation will not require any officer of the Board to make a judgement on the accuracy of the figures contained in the information section of the return. It is simply a question of taking the information provided by the taxpayer and using that information in the appropriate tax calculations.

- 2.39 It may be that a return without a tax calculation is submitted outside the required time limits. In strictness such a return would be incomplete. Even where in practice the Revenue might do the calculation in such cases, they will not guarantee to notify the taxpayer of any tax due before the due date. Interest and surcharge will be payable on any tax paid late.

**A calculation made by the Revenue will be treated as if it were a self-assessment made by the taxpayer**

- 2.40 Any calculation made by the Revenue, rather than the taxpayer, will be treated as if it were a self-assessment for all other purposes.

**Corrections of errors or mistakes in the return**

**Section 9(4), (5) & (6)**

- 2.41 An officer of the Board may amend a self-assessment to correct ('repair') any '*obvious errors or mistakes in a return*' at any time during the 9 months following the date on which the completed tax return was filed with the Revenue. For example amendments may be made to correct arithmetic errors, or errors of principle. These corrections will be made whether they increase or reduce the tax due. Where there is an increase in tax, penalties could arise if the return was shown to have been submitted fraudulently or negligently.

The process of repair will not require any officer of the Board to make a judgement on the accuracy of the figures contained in the information section of the return. It is simply a question of replacing an incorrect calculation based on the information provided by the taxpayer with the correct calculation based on that same information. If the information *itself* is incorrect then it can only be corrected by the Revenue through enquiry, not repair.

- 2.42 Similarly, the taxpayer may wish to amend the information originally entered in the return (for example to replace an estimate with an accurate figure), and to make corresponding amendments to the self-assessment. The taxpayer will be allowed to notify and make any such amendments at any time during the 12 months following the filing date. (*But this right is suspended if the return is under enquiry - see para 2.45.*)
- 2.43 Although there is a 9 month time limit for Revenue 'repairs' it is expected that most repairs will be made in the initial processing shortly after the filing of the return to the Revenue. If an error is not corrected within this 9 month period it cannot be corrected by the Revenue unless a formal enquiry is opened into the return (*see Chapter 4*).
- 2.44 Where a taxpayer disagrees with a 'repair' made by an officer of the Board and, exceptionally, the matter is not resolved by correspondence, the taxpayer is entitled to amend the return back to its original state (*but again subject to para 2.45*). In such cases the Revenue could only pursue the matter by means of a formal enquiry.
- 2.45 But the taxpayer may not formally amend a self-assessment during any period in which the corresponding return is under enquiry. (The taxpayer will have the right to make appropriate amendments once the enquiry is complete: *see Chapter 4*.)
- 2.46 Although the time limit for repairs by the Revenue is set by the actual date on which the return is filed, the time limit for amendments by the taxpayer is set by the statutory filing date. So if the return is filed late the time in which the taxpayer can make amendments is correspondingly reduced.

2.47 Where an error is discovered after the time limit for repairs (or an amendment) has passed, action may nonetheless be taken to correct it. Where the error has resulted in an overpayment of tax it may be covered by a claim to error or mistake relief (*see paras 2.62 to 2.64*). Where the error has resulted in an underpayment of tax it may be open to the Revenue either to commence an enquiry, or make a discovery assessment, depending on the time at which the error is discovered (*see Chapter 4*). Where taxpayers become aware of an underpayment after the expiry of the time limit for amendments, they should notify the Revenue so that corrective action may be taken accordingly.

#### **Other rules unchanged**

2.48 The requirement to make a declaration that the tax return is to the best of the taxpayer's knowledge '*correct and complete*' is unchanged (S.8(2) TMA 1970).

2.49 Similarly the general rules regarding the extent of the information required in the return are unchanged (S.8(3) & (4) TMA 1970). So the return may require information relating to different periods, different sources of income, and to more than one person.

#### *Time limits for self-assessment procedure*

#### **Time limits will normally be set by reference to the annual filing date**

##### ***Section 34(1)***

2.50 The time limits for making a self assessment broadly follow the old rules for Revenue assessments, but are set by reference to the filing date. As the filing date for any year is 31 January following the tax year to which it relates the taxpayer has a total of 5 years 10 months from the end of the relevant tax year in which to make a self-assessment. (This is without prejudice to the time limits in **Section 8** (*see para 2.15*) and any penalties for failure to meet them (*see paras 2.67 to 2.79*.) After this time limit has passed tax can only be assessed by means of a Revenue assessment (*see para 4.102*).

2.51 In certain exceptional circumstances the self-assessment time limit may be extended by up to 12 months (*see para 2.88*).

#### *Information to be included in the return*

#### **Specification of information required in a Self Assessment return**

2.52 The information required in Self Assessment returns will be similar to that required in existing returns. It will be such information '*as may reasonably be required*' (**Section 8(1)(a)**) and will include information needed by the Revenue to check that the self-assessment is correct. For example it will include all the information needed to calculate the tax due on the taxpayer's total income and any chargeable gains, for the period covered by the tax return. This will be true whether the calculation is made by the taxpayer or by the Revenue.

## Use of provisional figures in returns

- 2.53 There will be occasions on which some information cannot be finalised within the formal self-assessment time limits despite the taxpayer's best efforts to do so. In such cases the taxpayer should include a 'best estimate' of the information in the return and, if appropriate, a corresponding estimate of the tax due. The estimate should be clearly identified as such in the return and where appropriate should be accompanied by a note saying how the estimate was calculated and when the final figure is likely to be available. A return containing any such provisional figure will not be regarded as incomplete.

A return containing a blank entry, or an entry in the form 'to be agreed', instead of a numerical estimate will be incomplete and could result in a penalty for late filing. Therefore a return containing an estimate should only be submitted once it is clear that a more accurate figure will not be available before the filing date.

- 2.54 Once the correct figure is available it should be notified to the Revenue without delay, together with any amended self-assessment. If there is unreasonable delay in submitting the correct information, and there is additional tax to pay, the Revenue would be able to charge a penalty (up to the amount of the additional tax) on the basis that the original estimate was insufficient. This penalty could be sought even if the original return had not been submitted negligently. (S.97(1) TMA 1970).

## Use of judgmental figures, for example valuations, in returns

- 2.55 Valuations necessarily require the exercise of judgement, and more than one figure may be equally sustainable. Where necessary taxpayers should enter valuations in their returns, indicating how they have been reached. If the figure is provisional it will be treated as in *paras 2.53 and 2.54*. But if it is a considered figure it will be regarded as the final figure subject to the Revenue right to enquire into the return (*see Chapter 4*) and the taxpayer's right to amend the return (*paras 2.42 and 2.60*) or to make a claim to error or mistake relief (*paras 2.62 to 2.64*).

## Further guidance on estimates and valuations

- 2.56 The Inland Revenue intend to issue a more detailed statement on estimates and valuations before 1997.

## Informal advice and uncertainty

- 2.57 Taxpayers needing guidance on completing any aspect of a return should seek help from their Tax Enquiry Centre or Tax Office.
- 2.58 But there may still be some occasions when the taxpayer is uncertain as to the accuracy or completeness of some aspect of the return. In any such case the taxpayer should complete the return on the basis that appears most appropriate and should include full details of the points on which they are uncertain in the return. If they do this and the return is checked at a later stage, they will not be penalised if they were wrong, provided their original view was reasonable and they had disclosed all the relevant facts.

## Inland Revenue Rulings

- 2.59 It is intended that the informal provision of guidance should be supported in appropriate cases by a new formal procedure under which taxpayers can seek binding rulings on completed transactions from the Revenue before completing their tax returns. The first proposals on this procedure were announced in the consultative document 'Post Transaction Rulings' published in May 1994.

## **Inaccuracies in the return**

- 2.60 As now, taxpayers must take reasonable care to complete returns correctly. Innocent mistakes will not be penalised. Provided the return is sent in on time there will be a year in which a taxpayer can amend it (unless the right to amend the self-assessment has been suspended pending the completion of an enquiry: *see para 2.45*).
- 2.61 But of course errors arising from fraudulent or negligent conduct will be subject to penalties.

## **Error or mistake relief claims will still be possible**

### ***Section 33(1)***

- 2.62 In addition to the right to amend the self-assessment within 12 months of the filing date (*para 2.42*) the taxpayer will still be entitled to make a claim to 'error or mistake' relief within 5 years of the annual filing date for the year concerned. The general conditions for such claims are unaltered.

### ***Section 33(2)***

- 2.63 However, as now, no claim will be possible if the claim is in respect of
- an error or mistake concerning the basis on which the returned tax liability was calculated, and that basis was the generally prevailing practice at the time the return was made, or
  - an error or mistake in a claim that was included in the return. (There are separate procedures for making such claims - *see Chapter 6*)
- 2.64 So a taxpayer will not be able to claim error or mistake relief simply because the Revenue announces that it has changed its practice in relation to the treatment of some particular item.

# Sanctions against a failure to file a return

## *Introduction*

- 2.65 Clearly Self Assessment would not work unless there were rules to penalise those taxpayers who fail to file a return on time, and rules that allowed the Revenue to establish a tax charge in the absence of a completed self-assessment.
- 2.66 The sanctions will be
- penalties for a failure to file a return on time
  - a rule allowing the Revenue to make a determination of the tax due. This determination will be treated as a self-assessment for all purposes until such time as the taxpayer files an actual self-assessment.

## *Penalties for failure to file a return on time*

**There will be both automatic and discretionary penalties for failure to file a return on time**

### ***Section 93***

- 2.67 If the time limits for the filing of tax returns are not met fixed penalties will automatically arise. In more substantial cases additional daily penalties may be sought. And in cases of serious delay tax geared penalties may become due.

### **Fixed penalties**

#### ***Section 93(2) & (4)***

- 2.68 The initial penalty is fixed at £100. If the return is still outstanding 6 months after the filing date there will be a further penalty of £100 *unless* an officer of the Board has already applied to the Commissioners for a daily penalty (*see para 2.73*). These fixed penalties will be determined by an officer of the Board (***Section 100***).

### **Example: fixed penalties for late filing of tax return**

- 2.69 The filing date for a 1996/97 tax return issued in April 1997, requiring a return of income for year ended 5 April 1997, is the annual filing date of 31 January 1998 (***Section 8(1A)***).

If the return is filed on or before 31 January 1998 no penalty is due.

If the return is filed on 10 April 1998 it is filed after the annual filing date. A fixed penalty of £100 will have been imposed once the filing date had passed. (***Section 93(2)***)

If the return is filed on 10 August 1998 (i.e. more than 6 months after the formal filing date) then a further fixed penalty of £100 will have been imposed, making £200 in all (providing no application for a daily penalty has already been made: *see para 2.73*). (***Section 93(4)***)

## **Restriction of fixed penalties where tax due minimal**

### ***Section 93(7)***

2.70 The general rule is that the fixed penalties apply to all cases of late filing, regardless of the tax at stake. However they cannot exceed the tax liability for the year. So in cases in which the tax due is less than £100 (or £200 as appropriate) the penalties will be reduced.

### **Example: restriction of fixed penalties where tax due minimal**

2.71 Consider the return filed on 10 August 1998 in *para 2.69*.

If the tax due is £7,500 the fixed penalties of £200 will be due in full. (*Section 93(7)* does not apply)

If the tax due is £750 the fixed penalties of £200 will be due in full. (*Section 93(7)* does not apply)

If the tax due is only £150 the fixed penalties will be reduced to £150. (*Section 93(7)* applies)

## **Appeals against the determination of a fixed penalty**

### ***Section 93(8)***

2.72 The taxpayer may appeal against the determination of any fixed penalty by an officer of the Board. But the Commissioners can only set the penalty aside if the taxpayer had a reasonable excuse for the failure that occurred during the period between the filing date and the submission of the return. Any such reasonable excuse must apply for the whole period of default. It will not be sufficient for there to have been a reasonable excuse for part of the period.

## **Where the tax at risk is substantial daily penalties may be determined**

### ***Section 93(3) & (6)***

2.73 In addition to the fixed penalties a daily penalty of up to £60 per day may be determined if leave is given by the Commissioners (although if any such penalty is determined within 6 months of the fixed filing date the second penalty of £100 no longer applies).

2.74 It is intended to use this sanction where the tax at risk is believed to be high and therefore the fixed penalties may be an insufficient deterrent.

2.75 Daily penalties will only apply if an officer of the Board obtains a direction by the General or Special Commissioners. When that direction has been obtained daily penalties will be imposed by the officer of the Board and will apply for each day on which the failure continues following issue of the notice of the direction.

### ***Section 93(6)***

2.76 A daily penalty cannot be imposed if the return is filed before the determination of that penalty.

## And tax geared penalties may be determined in serious cases of delay

### *Section 93(5)*

2.77 If the failure to file the return continues for more than 12 months after the filing date an officer of the Board may impose a tax geared penalty. This penalty cannot exceed the tax liability for the year and may be subject to mitigation by the Board.

## Right of appeal against penalty determinations

### *Section 100B*

2.78 Although the right of appeal against the determination of a fixed penalty under this section is limited by *Section 93(8)* to grounds of 'reasonable excuse' (*para 2.72*) the taxpayer will continue to have the normal rights of appeal against any tax geared penalties sought under *Section 93*.

## Example: daily and tax geared penalties

2.79 The filing date for a 1997/98 tax return issued in April 1998, requiring a return of income for the year ended 5 April 1998, is the annual filing date of 31 January 1999 (*Section 8(1A)*).

Consider a taxpayer whose self-assessment for the previous year showed a net tax liability for the year of £25,000.

If the return is still outstanding on 1 March 1999 a fixed penalty of £100 is due (since 1 February) (*Section 93(2)*).

But in view of the tax at stake an officer of the Board may already have decided to apply to the Commissioners for a daily penalty. Assume that on 31 March 1999 the Commissioners make a direction that the officer of the Board may impose a daily penalty of £10 and the taxpayer is notified accordingly (*Section 93(3)*).

If the return is still outstanding at 31 August 1999 the additional daily penalties total £1,540 (£10 for each day between 1 April 1999 and 31 August 1999). Although the delay is now more than 6 months an additional fixed penalty is not due (*Section 93(4)(b)*).

If the return is still outstanding at 28 February 2000, and assuming that the daily penalty has not been increased, the additional daily penalties now total £3,340 (£10 for each day between 1 April 1999 and 28 February 2000). The delay is now more than 12 months and a tax geared penalty is due (since 1 February 2000) in addition to the fixed and daily penalties already determined (*Section 93(5)*).

## *Determination of self-assessment where return not filed*

### *Section 28C*

2.80 Without a completed return the Revenue will not know what tax to collect for the relevant year, or what payments on account are required for the following year.

2.81 In such cases the Revenue will have to make some form of estimate of the tax due. But the new mechanism must avoid the problems generated by estimated assessments made under the current rules.

2.82 The solution is a determination of the tax due which will be treated as a self-assessment but only **until such time as the taxpayer files an actual self-assessment**. The taxpayer's self-assessment automatically replaces the determination without the need for an appeal or arbitration.

#### **Determination of tax due**

##### ***Section 28C(1)***

2.83 Where a self-assessment return is not filed on or before the appropriate filing date an officer of the Board may make a determination of the tax due. This determination must be made *'to the best of his information and belief'*.

#### **Notice to be served on the taxpayer**

##### ***Section 28C(2)***

2.84 Notice of the determination must be served on the taxpayer, stating the date of issue.

#### **The determination will be treated as a self-assessment until such time as the actual self-assessment is filed**

##### ***Section 28C(3)***

2.85 The determination will be treated as a self-assessment until such time as the taxpayer files the actual self-assessment for the relevant tax year. There is no right of appeal against the determination. But once the actual self-assessment is filed it automatically replaces the determination. The tax charged by such a determination is payable and enforceable until it is replaced by a self-assessment, at which point any tax overpaid will be repaid.

2.86 The due date for payment of the tax charged by the determination is the due date that would have applied if the self-assessment had been filed on time. This tax will also set the level of the payments on account required for the following year.

##### ***Section 28C(4)***

2.87 Any recovery proceedings underway at the time the actual self-assessment is filed may continue, but with the substitution of the estimated amount by the sum shown in the taxpayer's self-assessment.

#### **Time limits for determinations and subsequent self-assessments**

##### ***Section 28C(5)***

2.88 No determination can be made after the normal 5 year limit for self-assessments. The determination can only be replaced by an actual self-assessment made within that time, or if later, within 12 months of the date of the determination.

# Other taxpayer obligations

## *Requirement to notify chargeability*

**Taxpayers who do not receive a tax return will still be required to notify chargeability to income tax or capital gains tax**

### *Section 7(1)*

- 2.89 Self Assessment is a system for dealing with tax returns. So it will only apply to taxpayers who have been identified as requiring a tax return, whether for 1996/97 or any subsequent year, and who have been issued with a Self Assessment return.
- 2.90 The Revenue will not always be able to identify who needs a return so the requirement to notify chargeability will remain under the new system. Any person who has not been required to complete a tax return but who nonetheless has profits or chargeable gains on which tax is due must notify an officer of the Board that they are chargeable to tax.

### **Time limit for notification will be reduced to 6 months**

- 2.91 The time limit for notifying chargeability will be 6 months from the end of the tax year in which the tax liability arises. This compares with the current 12 month time limit.
- 2.92 The new 6 month time limit ensures that the taxpayer can be sent a tax return in sufficient time for it to be completed within the normal return cycle for the year.

### **Exceptions to the requirement to notify chargeability**

#### *Section 7(3) to (7)*

- 2.93 As now there will be exceptions to this requirement. These are where the taxpayer
- has no chargeable gains (or such gains as there are do not exceed the annual exempt amount) and *either*
  - has no net liability to income tax for the year, *or*
  - has had sufficient tax deducted at source to meet the net income tax liability for the year.

### **Further guidance on the requirement to notify chargeability**

- 2.94 The Inland Revenue intend to issue a more detailed statement on the requirement to notify chargeability in due course.

### **Penalties for failure to notify chargeability**

#### *Section 7(8)*

- 2.95 The taxpayer will be liable to a financial penalty if notification is not made within the 6 month time limit. This penalty will be calculated by reference to the net tax due, but unpaid, at 31 January following the tax year in which the liability arises.
- 2.96 This means that even if notification is made after the 6 month time limit the penalty can be eliminated if the taxpayer pays the full amount of the tax due on 31 January. Where any penalties do arise they will be subject to mitigation as at present.

## Time at which new rule applies

### para 1(2), Schedule 19 FA 1994 (as amended by para 1, Schedule 21 FA 1995)

2.97 The new *Section 7* first applies in respect of 1995/96. So any notifications for that year must be made by 5 October 1996 unless a return, or an assessment, has already been issued for that year.

### *Requirement to keep records on which return is based*

## Taxpayer must keep and preserve records relevant to tax liability

### *Section 12B(1)*

2.98 Under Self Assessment taxpayers will be required both to keep and preserve the records needed to make a correct and complete return for any period.

2.99 This requirement comes into effect for the tax year 1996/97. Many businesses will have a basis period for 1996/97 that is a long (24 months or more) transitional period between the old 'preceding year basis' and the new 'current year basis'. For such businesses the first accounting period for which records must be kept may be a period commencing in 1994/95.

2.100 It is virtually impossible to produce an accurate return of profit without keeping records of one sort or another. Many taxpayers will already be keeping records, often for business management purposes and general reasons of prudence if not specifically for tax purposes. But the formal requirement to keep records should discourage taxpayers who might otherwise choose not to keep or retain records of an adequate standard in the hope that the Revenue would then only have evidence to support a relatively low estimate of profits made.

## Period for which records must be kept

### *Section 12B(1)(b) & (2)*

2.101 Where a return is issued at the normal time the relevant records must be kept until the later of

- the date on which a formal enquiry into the return is treated as complete (*see Chapter 5*);
- the date on which it becomes impossible for any such formal enquiry to be started;
- in the case of a taxpayer with a business the 5th anniversary of the annual filing date for the period covered by the return (the 5 year time limit applies to all records, not simply the business records);
- in any other case, the first anniversary of the annual filing date.

### **Section 12B(2A)**

2.102 Where a return is issued after the normal time, **but before**

- the 5th anniversary of the annual filing date for the period covered by return (in the case of a taxpayer with a business)
- the first anniversary of the annual filing date (in any other case).

the record keeping requirement is the same as that in *para 2.101*.

2.103 But where the return is not issued **until after** the dates given in *para 2.102* the record keeping requirement only extends **to those records still in the taxpayer's possession at the time the return is received**. These will be the only records, if any, that the taxpayer uses to complete the return. Any such records must then be kept until the later of

- the date on which a formal enquiry into the return is treated as complete;
- the date on which it becomes impossible for any such formal enquiry to be started.

For example, most employees are correctly taxed under PAYE and do not need to be issued with returns each year. Where, exceptionally, an employee is issued with a return after the first anniversary of the annual filing date he or she would only be expected to retain those records used when completing the return.

### **Business records to be kept**

#### **Section 12B(3) & (6)**

2.104 In the case of a business (including the business of letting a property) the records that must be kept include records of

- all receipts and expenses
- all goods purchased and sold
- all supporting documents relating to the transactions of the business, that is accounts, books, deeds, contracts, vouchers and receipts (and computer records - S.127 FA 1988).

### **Other records to be kept**

2.105 There are no specified rules for other sources of income other than the general requirement to make a complete and correct return. But typically taxpayers will be expected to keep evidence of the income that they have received, such as bank statements or dividend vouchers. Employees will need to keep their P60s and evidence of the taxable benefits they have received. Where someone returns a chargeable gain (or loss) they will need to keep all the records relating to the asset in question and the calculation of the gain (or loss) on its disposal.

## Further guidance on the records to be kept

2.106 Following a period of consultation the Inland Revenue intends to publish further guidance and advice on these new rules. In practice penalties will not be sought in respect of record keeping failures that take place before that advice has been published and until a reasonable period of time has been allowed for taxpayers and their advisors to assimilate the guidance and make any necessary changes to their record keeping systems and procedures.

## Records may be preserved as copies of the originals

### *Section 12B(4)*

2.107 Providing all the original information is retained it may be retained in a form other than the original documents. This allows original documents to be retained as copies, including copies maintained in electronic form on computer based optical imaging systems providing the images that are retained are complete and full copies.

## Penalty for failure to keep records as required

### *Section 12B(5)*

2.108 A penalty of up to £3,000 may be charged for each failure to keep or to preserve adequate records in support of a return.

2.109 Where record keeping failures come to light during the course of Revenue enquiries, they are likely to be a factor to be taken into consideration in determining the extent to which any penalties are to be mitigated in respect of other offences, for example where incorrect accounts have been submitted and a penalty is sought under Section 95. Where the record keeping failure is taken into account in this way, a penalty under this section will normally be sought only in serious and exceptional cases where, for example, records have been destroyed deliberately to obstruct an enquiry or there has been a history of serious record keeping failures.

2.110 The taxpayer will have the right of appeal against the determination of any such penalty.

## Failure to keep records on which a claim is based

### *Section 12B(5A)*

2.111 Where a particular claim, election or notice can only be made in a return any failure to retain the records relating to that claim etc. falls within the terms of *Section 12B(5)*. But where the claim etc. could have been made independently of a return then a failure to retain the relevant records falls within the terms of *Schedule 1A* (see Chapter 6).

## *Conversion table*

### **TMA 1970**

#### ***Section 7***

(operation in 1995/96)

#### ***Section 8(1)***

#### ***Section 9***

S.11A TMA 1970

#### ***Section 12B***

#### ***Section 28C***

#### ***Section 33***

#### ***Section 34(1)***

#### ***Section 93***

#### ***Section 100B(1)***

as substituted by

as amended by  
as substituted  
and amended by  
as substituted  
and amended by

repealed by  
as inserted by

as inserted by  
as amended by  
as amended by  
as substituted by  
as amended by

### **FA 94 and FA 95**

para 1, Schedule 19 FA 1994 and  
Section 115(1) FA 1995  
para 1, Schedule 21 FA 1995  
Section 178(1) FA 1994 and Section  
104(1), (2) and (3) FA 1995  
Section 179 FA 1994, Section  
104(4) FA 1995 and Section  
115(2) FA 1995  
Section 115(3) FA 1995  
para 3, Schedule 19 FA 1994 and  
Section 105 FA 1995  
Section 190 FA 1994  
para 8, Schedule 19 FA 1994  
para 10, Schedule 19 FA 1994  
para 25, Schedule 19 FA 1994  
para 31, Schedule 19 FA 1994

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## *Introduction*

### **Outline of the present payment system**

- 3.1 The current system for the payment of income tax and capital gains tax requires the Revenue to create a legal charge to tax by making an assessment. Once this charge has been created the taxpayer is required to pay the tax due on the date (or dates) specified in the assessment.
- 3.2 So, for example, an assessment to tax arising under Case I of Schedule D is normally issued during the months of August to October of the tax year to which the assessment relates. The tax due is payable in two instalments, the first on 1 January in that tax year and the second on 1 July following.
- 3.3 But an assessment on taxed income, or to capital gains tax, requires the tax to be paid in one instalment, on 1 December following the tax year. So whenever taxpayers have more than one assessment for any year they will also have more than one tax bill, and more than one payment date.
- 3.4 An assessment contains a formal demand for the first instalment of tax to be paid by the appropriate due date. The taxpayer can make the payment either by cheque or by using the bank giro system through any bank or post office. The Collector of Taxes issues another demand prior to any second instalment becoming due and this can be paid in the same way.
- 3.5 Interest can arise on any tax which although charged by an assessment is not paid at the required time. The interest is charged on any amount outstanding between the date on which the tax was originally due and payable (the reckonable date) and the date on which it is finally paid in full (S.86 TMA 1970).
- 3.6 Where any of the tax charged by an assessment is in dispute, and the assessment is under appeal, the taxpayer may apply to postpone collection of the amount of tax in dispute. In such circumstances the reckonable dates are revised (S.86 TMA 1970).
- 3.7 There are special rules for interest that arises on tax charged by an assessment to make good a loss of tax due to any failure or error on the part of the taxpayer, whether innocent or otherwise (S.88 TMA 1970).
- 3.8 The interest paid on repayments of tax is known as "repayment supplement" (S.824 ICTA 1988). But interest will only be added to a repayment of tax that is made more than 12 months after the end of the year of assessment to which it relates.
- 3.9 A similar "12 month" rule applies to repayments of tax made to employers and contractors for overpaid PAYE or subcontractor deductions (S.203(2)(dd) ICTA 1988).
- 3.10 The rates of interest that apply on tax charged are set by Regulations (S.178 FA 1989).

### **Outline of the new payment system**

- 3.11 Under the new system the obligation to pay tax will not be linked to the issue of an assessment. Instead the taxpayer will be automatically required to make two payments on account towards the tax due for any year and then a third and final 'balancing payment' to meet any tax still outstanding at the annual filing date for the Self Assessment return.

- 3.12 The payment scheme will cover all income and capital gains tax due. So there will be a single set of payment dates for all sources of income, and a single tax bill for the year. (Indeed it is intended that the taxpayer should have a single charge account. Statements will be issued showing all payments made, and all liabilities outstanding.)
- 3.13 The first payment on account will be due on 31 January of the tax year in question (i.e. the annual filing date for the *preceding* year). The second payment on account will be due on the following 31 July, and any balancing payment on the next 31 January (i.e. the annual filing date for that year).
- 3.14 The intention is that each payment on account should be approximately one half of the income tax liability for the year. They will be calculated by reference to the *previous* year's income tax liability, and will be reduced to give credit for tax deducted at source. Capital gains tax will only be included in the balancing payment.
- 3.15 Taxpayers will have the right to claim to reduce or cancel payments on account where they have grounds for believing that payments based on the tax liability for the previous year will lead to an overpayment of tax in the current year.
- 3.16 The main exceptions to the general scheme will be where the self-assessment is amended after the filing date, or where the Revenue raises a discovery assessment (*see Chapter 4*). In such cases the additional tax will be due 30 days after its notification to the taxpayer. Where a return is issued late the balancing payment will be required 3 months after the issue of the return.
- 3.17 Interest will be charged on any amount of tax unpaid at the due date for payment, whether that tax is due as a payment on account or as a balancing payment. In the case of an amendment to a self-assessment made after the filing date, or to a discovery assessment, the interest charge will run from the annual filing date for the relevant tax year.
- 3.18 The "12 month" rule for repayments of tax will no longer apply. Instead interest will be paid on *any* overpayments of tax, whether payments on account or balancing payments (subject to certain conditions), and will be calculated simply by reference to the due date for the relevant payment (or, if later, the date on which the tax was paid). The same principle will apply to repayments of overpaid PAYE tax or subcontractor deductions, which will be deemed to be paid on 31 January following the tax year to which they relate.
- 3.19 There will be new rules for interest charged (or paid) following adjustments for reliefs and deductions carried back to earlier years. These rules will follow those introduced for companies under Pay and File (S.87A TMA 1970 and S.826 ICTA 1988).
- 3.20 In addition to any interest that may arise on tax paid late there will also be a fixed penalty or "surcharge" to encourage prompt payment. The surcharge will initially be 5% of any payment still outstanding 28 days after the appropriate due date, rising to a maximum of 10% of the tax unpaid 6 months after the filing date.
- 3.21 Taxpayers will be able to appeal against the imposition of a surcharge on the grounds of having a reasonable excuse for late payment.
- 3.22 Interest will be charged on all late payments of tax, surcharge or penalties. And any interest charge made will be added to the balance on the taxpayer's statement of account. The interest charge will be automatically updated whenever there is a change in the taxpayer's affairs, for example when a payment is made (*para 3.65 onwards*).

## *Payments on account*

**Payments on account will normally be required if the taxpayer was assessed to income tax in the preceding year**

### ***Section 59A(1)***

3.23 Payments on account will normally be required from any taxpayer who is assessed to income tax, of any amount, for the preceding tax year. This will be the case even if the assessment has not been made at the time the payments on account are due.

### **Calculation of the payments on account will take tax deducted at source into account**

3.24 The payments on account will not be calculated simply by reference to the total income tax assessed in the preceding year, but by reference to "*a relevant amount*" of the income tax assessed. The relevant amount is the amount by which the total income tax assessed exceeded the credits for tax deducted at source.

### **No payments on account will be required if the relevant amount is below a certain limit**

3.25 Where the relevant amount is below a certain limit no payments on account will be required. The limit that applies in any case will be defined as the higher of

- a fixed amount of tax
- a fixed proportion of the assessed tax.

The precise value of these limiting criteria will be set by regulations in due course. These limits will be set at a level that ensures that most employees and pensioners (and others who receive the bulk of their income under deduction of tax or who have relatively small outstanding tax liabilities) will not have to make payments on account. Instead such taxpayers will simply have to make one balancing payment after the end of the tax year (or will have the balancing payment collected through PAYE).

### **A payment on account can never exceed 50% of the relevant amount**

3.26 No taxpayer will be required to pay in either payment on account more than 50% of the relevant amount for the preceding year, even though it may already be clear, at the time the payments are made, that the actual liability for the year will exceed that for the preceding year.

### **No payments on account will be required in respect of capital gains tax**

3.27 Capital gains tax is specifically excluded from the computation of payments on account because of the irregular nature of such gains. So any capital gains tax liability will simply be payable as part of the balancing payment on 31 January following the tax year.

## Definition of income tax 'deducted at source' for the purposes of Section 59A

### Section 59A(8)

3.28 When computing the "relevant amount", or when claiming to reduce or cancel payments on account, the tax deducted at source should include

- any tax deducted (or treated as deducted) from any income, or tax treated as paid on any income
- any PAYE tax deducted at source (S.203 ICTA 1988) including any tax that will be deducted under PAYE in a subsequent year
- any tax credit on dividends etc. (S.231 ICTA 1988)
- any foreign tax credit relief (S.793(1) ICTA 1988).

Any amounts deducted at source under S.203 ICTA 1988 in a tax year in respect of a *previous year* should be excluded.

### Application to Class 4 NIC

3.29 References to payment of income tax apply equally to payments of Class 4 NIC. So in practice each payment on account will include a payment on account of the Class 4 NIC liability for the year.

### Example: calculation of relevant amount

3.30 A taxpayer's self-assessment for 1997/98 shows

Gross income tax assessed	£8,500
Gross capital gains tax assessed	£2,360
Gross Class 4 NIC	£650
SC60 tax deducted at source:	£1,750
Tax credits on dividends received:	£345

The relevant amount is income tax assessed for 1997/98  
less  
tax credits for 1997/98

The relevant amount of income tax for 1997/98 is therefore  
 $(8,500) - (1,750 + 345) = \mathbf{£6,405}$

The relevant amount of Class 4 NIC for 1997/98 is simply  
 $(650) - (0) = \mathbf{£650}$

No payment on account is required in respect of capital gains tax.

## Each payment on account will be equal to 50% of the relevant amount

### Section 59A(2)

3.31 The payments on account will each be equal to 50% of the relevant amount (unless the taxpayer makes a claim that they should be reduced: *see paras 3.36 to 3.54*).

## Due dates for payments on account

### Section 59A(2)

3.32 Whenever payments on account are required for any tax year they will be payable without demand

- the first on or before 31 January of that tax year, and
- the second on or before 31 July next following that tax year

3.33 Self Assessment tax returns will be designed to guide taxpayers through the calculation of payments on account etc. But in the same way that taxpayers can get Revenue assistance to calculate the overall tax liability there will be assistance to calculate the payments on account due. And although the Revenue will not be required to issue demand notices the Revenue will remind taxpayers that payments are due. Where possible the reminder will state the amount that is due, for instance at 31 July, and in Revenue calculation cases.

## Example: calculation of payments on account

3.34 Consider the example at *para 3.30*. The relevant amounts for 1997/98 were

income tax: **£6,405**

Class 4 NIC: **£650**

Therefore the payments on account required for 1998/99 are

**31 January 1999: £3202.50 + £325**

**31 July 1999: £3202.50 + £325**

## Collection of payments on account

### Section 59A(7)

3.35 The normal Self Assessment rules for the collection and recovery of income tax will apply to payments on account as they apply to the final balancing payment. Interest will be charged on any payments on account made late, from the due date for payment. Any tax not paid as a payment on account will automatically become due as part of the balancing payment for the year. A tax geared surcharge may be sought on any part of the balancing payment that is paid late (*see paras 3.84 to 3.110*).

## Claims to reduce or cancel payments on account

### Section 59A(3) & (4)

- 3.36 The payments on account required for any tax year are calculated by reference to the tax liability for the *preceding* year. For those taxpayers whose tax liability is relatively constant from year to year this method of calculation should ensure that the payments on account required approximate to the additional tax required over and above any tax deducted at source during the year.
- 3.37 But it is always possible that a taxpayer's circumstances will change significantly from one year to the next. In such circumstances it is possible that the payments on account, as originally calculated, will eventually result in a net overpayment of tax for the year.
- 3.38 In order to avoid overpayments of tax a taxpayer may make a claim to reduce or cancel the payments on account. Claims are required to ensure that the Revenue does not commence recovery proceedings to enforce payment for tax that will have to be repaid at the balancing payment date.

### Nature of claim

3.39 Any such claim should state the taxpayer's "*belief that*"

- there will be no income tax liability for the current tax year or that any such liability will be covered by income tax deducted at source, or
- the amount due for the current year, after taking into account tax deducted at source, will be less than the amount of payments on account based on the preceding year

and the claim should include the grounds for that belief.

3.40 The taxpayer will be able to make the claim in a tax return, in a claim form, or in writing. The Revenue has no power to reject such claims. But after processing any such claim will be reviewed to identify negligent or fraudulent claims.

### Time limit for claims

3.41 Claims must be made at any time before 31 January following the relevant tax year.

### Adjustments following claim

#### Section 59A(5)

- 3.42 Following any such claim the payments on account will be reduced or cancelled, as appropriate, to reflect the taxpayer's view of what payments on account, if any, are due for the current tax year.
- 3.43 If the payments have already been made any overpayment will be refunded, with interest.

### Example: adjustment following a claim to reduce payments on account

3.44 In *para* 3.34 payments on account for 1998/99 were calculated as

31 January 1999: £3202.50 + £325

31 July 1999: £3202.50 + £325

But it might be that in 1998/99 the taxpayer has more tax deducted at source than was the case in 1997/98. For example, if a higher proportion of all work carried out is subject to SC60 deductions the payments on account of income tax could be recalculated as follows:

Gross income tax assessed for 1997/98	£8,500
Tax credits on dividends received in 1997/98	£345
Estimate of SC60 tax deducted at source in 1998/99, say	£6,000

In the circumstances it would be reasonable to claim that the total amount to be paid as payments on account of income tax should only be

$$(8,500) - (6,000 + 345) = \mathbf{£2,155}$$

(The total payment on account of Class 4 NIC for 1997/98 is unchanged at **£650**)

So the revised payments on account are:

**31 January 1999: £1077.50 + £325**

**31 July 1999: £1077.50 + £325**

### Incorrect claims to reduce or cancel payments on account

#### *Section 59A(6)*

3.45 A penalty will be charged where a taxpayer fraudulently or negligently makes any incorrect statement in connection with a claim to reduce or cancel payments on account. The maximum penalty will be the difference between the amount that would have been paid but for the incorrect statement and the amount of the payments on account actually made. The penalty may be subject to mitigation by the Revenue, and on appeal, may be amended or cancelled by the Commissioners.

3.46 So for example if the claim that gave rise to the reduction considered in *para* 3.44 turned out to be false the maximum penalty would be

$$(6,405 + 650) - (2155 + 650) = \mathbf{£4,250}$$

3.47 A penalty cannot be sought in cases of innocent error, and will not be sought against a taxpayer who, in making the claim, acted in good faith

- but got the sums wrong (and had no reason to suspect that they were wrong), or
- acted on the basis of information that was correct at the time of the claim, but which subsequently changed.

3.48 The intention of this penalty is to prevent gross or persistent abuse. So the Revenue will seek to penalise those taxpayers who claim large reductions without any foundation or who, year on year, make claims under this section which result in them paying less than they should.

- 3.49 Once the return for the year is received the Revenue will look to see whether there is a significant difference between the amount of income tax that is shown to be due and the amount paid as reduced payments on account. Where there is a significant difference, or someone persistently claims excessively reduced payments on account, the Revenue will want to examine the grounds on which the claims were made and whether or not they were realistic, at the time, and made in good faith.

### **Changes to payments on account when 'relevant amount' not established until after the first date for a payment on account**

#### **Section 59A(4A) & (5)**

- 3.50 Where

- a self-assessment for the previous year is not made on time, *or*
- a self-assessment made at the normal time is amended

the correct 'relevant amount' will not have been established in time to be reflected in payments on account for the current year.

- 3.51 Where either of these situations applies the 'relevant amount' for the current year will have to be revised by reference to the final liability for the previous year as shown in the late self-assessment, or the amended self-assessment. A 'relevant amount' established at such time will be treated as if it had been established in a self-assessment made on the normal filing date for the previous year. Therefore the taxpayer will be required to pay any additional tax and interest due as the result of revisions to the payments on account.

#### **Example: adjustment to previous year and revision of relevant amount**

- 3.52 A taxpayer's self-assessment for 2010/11 is £3,000. Therefore the payments on account for 2011/12 are:

31 January 2012:	£1,500
31 July 2012:	£1,500

These payments are made on time, and in the correct amount. But after an enquiry into the 2010/11 return the liability for the year is revised upwards to £4,500. An amended self-assessment is made on 1 November 2012.

Each payment on account for 2011/12 is reset to £2,250, an increase of £750. Interest will arise on each underpayment until paid. The interest charge runs from the original due dates (31 January and 31 July 2012) until the date of payment.

#### **Direction by officer of the Board that payments on account are not required**

#### **Section 59A(9)**

- 3.53 An officer of the Board may direct that a taxpayer need not make any payments on account for a given year. Any such direction must be made before the normal filing date (31 January) for the year in question. And once such a direction has been made any consequential adjustments must also be made. For example, it might be necessary to repay any payment on account already made.

3.54 Directions under this section will be made to ensure that PAYE taxpayers who receive tax returns do not make payments on account when they are not needed. For example, it could be that an employee has some exceptional receipt that takes the relevant amount for a year above the de minimis limits described in *para 3.25*. Normally this would automatically trigger the payment on account rules for the following year. But if it is clear that payments on account are not necessary an officer of the Board can make a direction that no payments on account are in fact required.

### *Balancing payments*

**A balancing payment (or repayment) will be made to reflect tax liability calculated in the self-assessment for the year**

#### ***Section 59B(1)***

3.55 Apart from cases wholly dealt with through PAYE it will be exceptional if, in any year, the income tax paid at source and/or in payments on account is precisely equal to the actual income tax liability for that year. In most cases an additional payment (or repayment) of income tax will be required once the actual income tax liability has been calculated in the self-assessment return. In addition any capital gains tax due will be payable.

3.56 The additional tax will be due as a final balancing payment (or balancing repayment). The amount due will be the difference between

- the amount shown by the self-assessment included in the return, and
- the amounts already paid on account, together with
- any amounts deducted at source.

**Balancing payment will take tax deduction at source into account**

#### ***Section 59B(2) & (7)***

3.57 The calculation of the balancing payment must take into account *any* tax credits arising in the tax year to which the return relates. The tax credits allowed in the calculation of the balancing payment should include any tax to be coded out in a *future* year, but must exclude any amounts deducted at source during the year in respect of *previous* years.

3.58 And the tax deducted at source includes tax treated as deducted, or treated as paid on any income.

**Due dates for payment**

#### ***Section 59B(3), (4) & (5)***

3.59 The due date for payment depends on the precise way in which the charge arises. In the normal case the due and payable date will be the annual filing date for the year, 31 January next following the year of assessment.

3.60 But where a return is issued after 31 October following the tax year to which it relates, and there has been no failure to notify chargeability under **Section 7**, the due and payable date is 3 months from the date of issue of the return (again, the same as the normal filing date for such returns).

- 3.61 In any case for which an amended self-assessment has to be made (whether made by the Revenue or by the taxpayer) or where an assessment is made by the Revenue under **Section 29**, the due and payable date for additional tax that is not postponed is the later of the normal due dates given above, or 30 days from the date on which the notice of amendment is given.

**Example: calculation of balancing payments**

- 3.62 Consider a taxpayer whose self-assessment shows

Income tax assessed for 1998/99:	£7,450
Capital gains tax assessed for 1998/99:	£5,250
Class 4 NIC assessed for 1998/99:	£600

who has made payments on account as follows:

31 January 1999:	£4,500 (+ £275 in respect of NIC)
31 July 1999:	£4,500 (+ £275 in respect of NIC)

and who has tax credits of £640 for the year.

The balancing payments due on the annual filing date of 31 January 2000 are

	Tax	NIC
Income tax	7,450	
Capital gains tax	5,250	
Class 4 NIC		600
<b>less</b>		
payments on account	(9,000)	(550)
<b>less</b>		
tax credits	(640)	
Balancing payment required	<b>£3,060</b>	<b>£50</b>

**Interest charged on late payment of tax and paid on overpayments of tax**

- 3.63 Interest will be charged on unpaid balancing payments from the due date until payment. Similarly interest will be paid on any balancing *repayments*. In the case of balancing repayments the interest runs from the due date for payment (or, if later, the date of payment of the tax now to be repaid) to the date the repayment is made.
- 3.64 Any repayment (including interest) may be set off against the following year's payment on account.

# Automatic Interest And Surcharges

## *Interest charged on late payments of tax*

### **Interest will be charged on any tax paid late**

#### **Section 86(1) & (2)**

3.65 A charge to interest will automatically arise on any tax paid late, whether income tax, NIC or capital gains tax. So a charge to interest could arise in respect of

- any payment on account (**Section 59A**)
- any balancing payment (**Section 59B(3) or (4)**)
- any tax payable following an amendment to a self-assessment, whether made by the Revenue or the taxpayer (**Section 59B(5)**)
- any tax payable in a discovery assessment made by the Revenue (**Section 59B(6)**)
- any tax payable following a postponement (in relation to a discovery assessment or Revenue amendments to a self-assessment as the result of an enquiry: *see paras 4.84 & 4.105*) (**Section 55**)

### **Period for which interest charged**

#### **Section 86(1) to (3)**

3.66 For **payments on account and balancing payments** the interest will arise on any sums outstanding between **the due date for payment, and the date on which payment is finally made**.

For **amendments to self-assessments, and discovery assessments**, the interest charge will normally run from **the annual filing date for the relevant tax year** even though the due date for payment of the tax itself may be a later date.

The interest charge will arise from the due date even though that date may be a non-business day.

### **Rate of interest charged**

3.67 The rate of interest charged will be the rate set by regulations made under **Section 178 FA 1989**.

### **Special rules for interest on payments on account of income tax**

#### **Section 86(4) to (9)**

3.68 The normal interest charge on payments on account will arise on the difference between what is actually paid, and what *should have been paid*. In determining these amounts no account will be taken of any tax paid on account other than under **Section 59A(2)** or amounts payable as capital gains tax.

- 3.69 For example, if a payment of £3,500 should have been made on 31 July 1999, but only £2,500 is paid on that date, interest accrues on the balance of £1,000 from 1 August 1999 until the date on which the outstanding payment is finally made.
- 3.70 The amount that should have been paid for any payment on account can never exceed 50% of the relevant amount for the preceding year, even if the income tax for the current year, after taking into account tax deducted at source, exceeds the total of the payments on account. The taxpayer is under no obligation to increase the payments on account even when it is clear that they will be some way short of meeting the full tax liability for the year. So there can be no question of an interest charge on a payment on account simply because the overall liability for the current year has increased relative to the preceding year.

**Example: interest on payments on account and balancing payments**

- 3.71 A taxpayer's self-assessment for 2010/11 is £2,000. Therefore the payments on account for 2011/12 are:

31 January 2012:	£1,000
31 July 2012:	£1,000

The self-assessment for 2011/12 is £3,000 and any balancing payment is due on 31 January 2013.

Assume that:

- the payment of £1,000 due on 31 January 2012 is not paid until 1 April 2012;
- only £500 of the payment due on 31 July 2012 is paid at that date;
- the balancing payment of £1,500 due on 31 January 2013 is not paid until 1 March 2013

**Section 86 interest arises on**

- £1,000 for the 2 months 1 February 2012 to 31 March 2012
- £500 for the 6 months 1 August 2012 to 31 January 2013
- £1,500 for the 1 month 1 February 2013 to 28 February 2013

**Interest charges following an excessive claim to reduce payments on account**

**Section 86(4)**

- 3.72 Where there is a claim to reduce payments on account under *Section 59A(3)* or *(4)*, and following
- submission of the taxpayer's return and self-assessment for the current year, or
  - an enquiry into the return and self assessment for the previous year (on which the payments on account were originally based)

that claim proves to be excessive, there may be an underpayment of tax.

### Section 86(5) & (6)

3.73 This underpayment will be the difference between

- the amounts paid as a result of the claim, and
- the amounts that should have been paid *if the claim had been made in the correct amount*. The amount that should have been paid cannot exceed 50% of the relevant amount for the preceding year.

Interest will arise on any such underpayment of tax.

#### Example: interest charge following excessive claim to reduce payments on account

3.74 A taxpayer's self-assessment for 2010/11 is £4,000. Therefore the payments on account for 2011/12 are:

31 January 2012:	£2,000
31 July 2012:	£2,000

On the basis of a profit forecast at 31 December 2011 the taxpayer makes a claim to reduce these payments to £1,000 each. The reduced payments are both made on time.

When the 2011/12 return is filed on 31 January 2013 the self-assessment shows an income tax liability for 2011/12 of £3,750. The balancing payment of £1,750 is paid on 1 April 2013.

#### Section 86 interest arises on

- £875 for the 12 months 1 February 2012 to 31 January 2013
- £875 for the 6 months 1 August 2012 to 31 January 2013
- £1,750 for the 2 months 1 February 2013 to 31 March 2013

If the income tax liability for 2011/12 had been £5,600, and a balancing payment of £3,600 was paid on 1 April 2013, then **Section 86 interest would have been due on**

- £1,000 for the 12 months 1 February 2012 to 31 January 2013 (£1,000 is the maximum on which interest can be charged as 50% of the relevant amount for the previous year is £2,000, of which £1,000 was paid on account)
- £1,000 for the 6 months 1 August 2012 to 31 January 2013
- £3,600 for the 2 months 1 February 2013 to 31 March 2013

## Remission of interest charges on excessive payments on account

### Section 86(7) to (9)

3.75 It may well be that following

- submission of the taxpayer's return and self-assessment for the current year, or
- an enquiry into the return and self assessment for the previous year (on which the payments on account were originally based)

a taxpayer is entitled to a repayment of tax previously paid on account. But where those payments on account were never made, or appeared to be inadequate a **Section 86** interest charge will have arisen.

3.76 In such circumstances **Section 86** interest will only be chargeable on the amounts that should have been paid *if the claim had been made in the correct amount*. (Again, the amount that should have been paid cannot exceed 50% of the relevant amount for the preceding year.) Any existing interest charge on amounts in excess of the amounts that should have been paid will be mitigated.

### Example: remission of interest charge on excessive payments on account

3.77 A taxpayer's self-assessment for 2010/11 is £5,000. Therefore the payments on account for 2011/12 are:

31 January 2012:	£2,500
31 July 2012:	£2,500

After submitting the 2010/11 return the taxpayer realises that it contains an error. The first payment on account is paid in full, and on time, but the taxpayer decides not to pay any further amount until the liability for 2010/11 is settled. On 31 September 2012 it is agreed that the liability for 2010/11 is only £3,600. The taxpayer pays a further £1,100 on 1 November 2012

When the 2011/12 return is filed on 31 January 2013 the self-assessment shows an income tax liability for 2011/12 of £4,400. The balancing payment of £800 is paid on 1 March 2013.

If the payments on account had been based on the true liability for 2010/11 they would have been

31 January 2012:	£1,800
31 July 2012:	£1,800

### Section 86 interest arises on

- £0: the taxpayer is entitled to repayment supplement on £700 (2500 - 1800) for the 6 months 1 February 2012 to 31 July 2012
- £400 (1,100 - 700) for the 3 months 1 August 2012 to 31 October 2012
- £800 for the 1 month 1 February 2013 to 28 February 2013

## **Adjustments to interest charges**

3.78 Any adjustments to the interest charged will be made automatically, in the taxpayers statement of account. This statement will be updated whenever there is a change in the account, for example when an a payment is received. And the statement will include all interest charges, no matter how small.

### *Interest on tax charged in an assessment for 1995/96 (or earlier) made after 6 April 1998*

#### **New Section 86 interest rules will apply**

##### **Section 110 FA 1995**

3.79 The existing **Section 86** interest rules could have been retained for all assessments made for 1995/96 or earlier, even those made after Self Assessment has been introduced. But to simplify matters the new **Section 86** rules will also apply to any assessment for 1995/96 or earlier made after 6 April 1998. In any such case the due date for the assessment will be treated as being the 31 January following the tax year to which the assessment relates.

### *Interest paid on overpayments of tax*

#### **Section 824(1), 826 ICTA 1988 & 283 TCGA 1992**

3.80 Interest will be paid on any overpayment of any tax (or payments treated as tax) up to the statutory maximum that the taxpayer is required to pay.

3.81 The 12 month rule will no longer apply. Instead interest will be paid from the “relevant time” until the date of repayment.

#### **Section 824(3) ICTA 1988**

3.82 For repayments of tax the relevant time is defined as the later of the due date for the corresponding payment that is being repaid (e.g. an earlier payment on account or balancing payment), or the date on which the payment was in fact made.

3.83 For repayments of payments treated as tax, for example a penalty or surcharge, the relevant time is defined as the later of the due date for that payment (i.e. 30 days following the determination of the amount payable), or the date on which the payment was in fact made.

### *Surcharges on unpaid income tax and capital gains tax*

#### **A fixed penalty (“surcharge”) will arise on any tax paid late**

##### **Section 59C(1)**

3.84 The new Self Assessment system is based on voluntary compliance. So it is essential that those taxpayers who pay the right amount of tax at the right time feel confident that the system does not reward non-compliance in any way.

3.85 But the interest charged on late payments is not a penalty. It is designed to cancel the immediate financial advantage for those who pay late over those who pay on time.

- 3.86 So in addition to any interest that may arise on tax paid late there will also be a scheme of surcharges to encourage prompt payment. A surcharge will be payable in respect of any tax which
- is shown as due in any self-assessment (whether calculated by the taxpayer or the Revenue) but which is not covered by any payment on account or balancing payments made (*Section 59B*)
  - in the context of a formal enquiry is shown as due in an amended self-assessment, or discovery assessment, but which is not postponed pending an appeal (*Section 55 - see Chapter 4*).
- 3.87 The surcharge will also be payable on any Class 4 NIC unpaid as if it were income tax charged under Case I/II of Schedule D (S.16(1) Social Security Contributions and Benefits Act, 1992).

**The initial surcharge will be 5% of any tax unpaid after 28 days**

*Section 59C(2)*

- 3.88 Where a balancing payment is still unpaid more than 28 days from the due date for payment a surcharge will automatically arise. This initial surcharge will be equal to 5% of the tax unpaid at that date. This will include amounts that should have been paid as payments on account.
- 3.89 There will always be some taxpayers who intend to pay on time but, for some genuine reason, fail to do so. The 28 day period before a surcharge arises should ensure that these taxpayers do not incur such a charge.
- 3.90 There may also be some taxpayers who, having calculated their final liability for a tax year, realise that they will have insufficient funds to pay the balance due at the due date. The 28 day period will give these taxpayers time to contact the Revenue to arrange a suitable scheme of payment.

**There will be an additional 5% surcharge on tax still unpaid after 6 months**

*Section 59C(3)*

- 3.91 Any tax that remains unpaid more than 6 months from the due date for payment will be subject to a further surcharge. This further surcharge will again be equal to 5% of the unpaid tax.
- 3.92 The stepped surcharge is intended to provide an increasing incentive to pay tax that is late and to ensure that the tax due for one tax year is paid before the final tax due for the subsequent year.

### **Example: surcharge on late payment of tax due**

- 3.93 A taxpayer completes a self-assessment for 1998/99 showing a total tax liability of £9,000. The balancing payment due on 31 January 2000 is £5,500 but the taxpayer makes a payment of only £1,750. £3,750 is outstanding.

Interest will arise on the £3,750 from 31 January 2000 to the date of payment (**Section 86(1) & (2)**).

If the £3,750 is still outstanding at 29 February 2000 a surcharge of £187.50 is due (3750 @ 5%). (**Section 59C(2)**) If that surcharge is imposed on 1 March 2000 interest will run on the surcharge from 31 March 2000 until paid (**Section 59C(6)**).

If the £3,750 is still outstanding at 1 August 2000 a further surcharge of £187.50 is due (again 3750 @ 5%). (**Section 59C(3)**) If that surcharge is imposed on 1 August 2000 interest will run on the surcharge from 31 August 2000 until paid (**Section 59C(6)**).

### **Surcharges on additional tax payable on an amended self-assessment**

- 3.94 Although the tax due in a self-assessment may be increased following an amendment, whether made by the Revenue or the taxpayer, the due date for interest purposes remains the original due date. So any interest payable or repayable will be calculated by reference to the normal due date for the year regardless of the date of amendment.
- 3.95 But the due date for the *additional tax* payable is 30 days after the amendment. Surcharge is payable on any of the additional tax that remains unpaid 28 days *after that due date*.
- 3.96 So, for example, where an estimate is entered in the self-assessment, and the final figure becomes known some months later, no surcharge will be due providing the additional tax due is paid within 58 days of the amendment. But interest will run from the original due date.

### **No surcharge will be due if a penalty is determined in respect of the same tax**

#### **Section 59C(1)**

- 3.97 No surcharge will be payable on any tax on which a penalty is sought under **Sections 7, 93(5), 95 or 95A** in respect of the same tax. In such cases the Revenue will normally seek a penalty of at least the amount of the surcharge.

### **Interest will be charge on unpaid surcharge**

#### **Section 59C(6)**

- 3.98 A surcharge will be due for payment within 30 days of the date on which it is imposed. Interest will be charged on any surcharge paid late and will run from the end of the 30 day payment period until payment.

### **The surcharge will be imposed by a formal notice served on the taxpayer**

#### **Section 59C(5)**

- 3.99 An officer of the Board will be required to serve a notice on the taxpayer informing him that a surcharge is being imposed. This notice will state the day on which it was issued, and the time period within which an appeal can be made against the surcharge.

3.100 A separate notice will be required whenever a further surcharge is imposed.

### **Appeals against the imposition of a surcharge**

#### ***Section 59C(7) to (10)***

3.101 The taxpayer may appeal against a surcharge but must do so within 30 days of the date on which the surcharge was imposed.

3.102 In general the normal appeals procedures apply. But the grounds of appeal are confined to showing that the taxpayer had "*a reasonable excuse for not paying the tax*" on time.

3.103 If it appears to the Commissioners that throughout the "*period of default*" (that is the period from the due date to the day before that on which the tax was paid) the taxpayer had a reasonable excuse for not paying the tax then the surcharge will be set aside.

3.104 But if there was no reasonable excuse the imposition of the surcharge will be confirmed.

3.105 There is no formal definition of "*reasonable excuse*". But an inability to pay the tax due "*shall not be regarded as a reasonable excuse*".

### **Mitigation of surcharge**

#### ***Section 59C(11)***

3.106 The Board of Inland Revenue will have a discretionary power to mitigate or remit any surcharge.

3.107 So, for example, if there was reasonable excuse for non payment of tax during part of a period of default the Board could use their discretionary power to ensure that the level of surcharge reflects the delay in the period after the reasonable excuse came to an end.

3.108 Similarly in any case in which an agreement has been reached allowing the taxpayer to pay by instalments, those instalments would include interest. But the Board could use the power of mitigation to exclude surcharge, providing the instalment agreement was kept.

3.109 And the Board could use the power of mitigation to reduce or cancel the surcharge on the grounds of hardship.

### ***Surcharge on tax charged in an assessment for 1995/96 (or earlier) made after 6 April 1998***

#### **New surcharge rules will apply**

#### ***Section 109(2) FA 1995***

3.110 The new surcharge rules will apply to any income tax or capital gains tax assessment for 1995/96 or earlier made after 6 April 1998.

# Miscellaneous provisions

## **Changes to cash limit for magistrates' proceedings**

### *Section 65(1)*

3.111 Under Self Assessment tax, and other amounts due, can be recovered by way of proceedings in a Magistrates' court providing the total amount due does not exceed £2,000.

## **Interest will be charged on any sum due, including penalties and surcharge**

### *Sections 69 & 70(2)*

3.112 Once an amount has been added to the taxpayer's statement of account, whether as tax, a surcharge or a penalty, interest will be charged on sums unpaid. And for collection and recovery purposes all payments in the statement will be treated as tax due and payable.

## **Payments by cheque**

### *Section 70A*

3.113 From 6 April 1996 any payment made by cheque will be treated as having been made on the day the cheque is received (providing the cheque subsequently clears).

## **Rate of interest**

### *Section 178 FA 1989*

3.114 The rate of interest will be calculated using a formula to be set by regulations. Rates will change automatically when there is a change in the bank base rates.

The rate charged on late tax will be in line with the average rate for borrowing. The rate paid on overpaid tax will be in line with the average return on profits.

## **De minimis limits**

3.115 There will be no de minimis limits for interest. All amounts, no matter how small, will be added to the taxpayer's statement of account.

## *Payments on account: arrangements of the transitional year 1996/97*

### **Special rules for determining the payments on account required**

#### *Section 59A as modified by Schedule 21 FA 1995*

3.116 Because 1995/96 is a year of 'Revenue assessment' rather than self-assessment special transitional rules are required to determine the payments on account due for 1996/97.

3.117 The general principle is that the payments on account should be based on the overall tax liability for the previous year, and will be due in two instalments, one on 31 January 1997, one on 31 July 1997. A balancing payment (or repayment) will then be due on 31 January 1998 in the normal way.

3.118 But the tax due for 1995/96 may have been charged in a number of separate assessments, some requiring payment in two instalments, others requiring payment in one instalment, depending on the sources of income assessed. The special payment on account rules for 1996/97 continue the one instalment/ two instalment treatment for one final year by allocating the 1995/96 tax liability between 31 January 1997 and 31 July 1997 as follows:

- Case I/II Schedule D (and Class 4 NIC): **50% each**;
- Cases III to VI Schedule D: **all due 31 January 1997**;
- Schedule A: **all due 31 January 1997**;
- Higher rate tax (on taxed income sources): **excluded from calculation**;
- Tax deducted at source: **excluded from calculation**.

**Sections 59A(4) and (4A) as amended by paras 2(6) and (7) Schedule 21 FA 1995**

3.119 If the 1995/96 tax liability for any source of income is amended the payments on account will also be amended.

**Example: calculation of payments on account for 1996/97**

3.120 Olivia has various sources of income that give rise to a 1995/96 tax liability as follows:

Case II		4,000
Class 4 NIC		684
Case III	untaxed	1,000
	taxed	1,500
Case VI		915
Sch. A		1,000
Dividends	taxed	2,500
Capital gains tax		3,500
Higher rate tax (on taxed income)		2,400
<b>Total</b>		<b>17,499</b>

The payments on account required for 1996/97 are calculated as follows:

		<b>31 January 1997</b>	<b>31 July 1997</b>
Case II	4,000	2,000	2,000
Class 4 NIC	684	342	342
Case III (untaxed)	1,000	1,000	0
Case III (taxed)	1,500	0	0
Case VI	915	915	0
Sch. A	1,000	1,000	0
Dividends (taxed)	2,500	0	0
Capital gains tax	3,500	0	0
Higher rate tax (on taxed income)	2,400	0	0
<b>Totals</b>	<b>17,499</b>	<b>5,257</b>	<b>2,342</b>

### Direct collection arrangements for Schedule E taxpayers

3.121 A small number of Schedule E taxpayers currently pay their tax quarterly under the Direct Collection arrangements. These arrangements will last apply in 1995/96. For 1996/97 and subsequent years these taxpayers will be issued with tax returns and required to self-assess in the normal way. The Inland Revenue will calculate any payments on account required for 1996/97 and will advise taxpayers accordingly.

### De minimis limits

3.122 De minimis limits will apply for payments on account due for 1996/97 in the normal way (*para 3.25*).

### Special rules for giving partners credit for the tax paid against a composite partnership assessment for 1996/97

#### *para 3 Schedule 21 FA 1995*

3.123 In 1996/97 partners will be required to include a self-assessment of their total income in their tax returns, including any partnership income. But a composite partnership assessment will still be required for any partnership not yet within the new current year basis of assessment.

3.123 Where a partner's share of partnership profits is assessed as part of a composite partnership assessment for 1996/97 that partner must be given a corresponding credit to include in his self-assessment. Otherwise that share of profits would be assessed twice. For the purposes of the partners self-assessment for 1996/97 the tax paid by the partnership on a partner's share of partnership profit **will be treated as if it were tax deducted at source**.

3.124 This rule only applies for the purposes of the partners self-assessment for 1996/97 and for no other purpose. Therefore, when calculating the partner's payments on account for 1997/98 **only genuine tax credits should be used in the determination of the 'relevant amount' for the previous year, 1996/97**.

3.125 No claim under S.32 TMA 1970 (relief from double assessment) will be allowed in respect of that income for that year.

## *Conversion table*

### **TMA 1970**

#### ***Section 59A***

(operation in 1996/97)

#### ***Section 59B***

(operation in 1996/97  
for partners)

#### ***Section 59C***

#### ***Section 65(1)***

#### ***Section 69***

#### ***Section 70(2)& (3)***

#### ***Section 70A***

#### ***Section 86***

### **ICTA 1988**

#### ***Section 824***

#### ***Section 826***

### **FA 94 and FA 95**

as inserted by

as amended by

as inserted by

as amended by

as inserted by

as amended by

as amended by

as amended by

as inserted by

as substituted by

Section 192 FA 1994 and  
Section 108 FA 1995

para 2, Schedule 21 FA 1995

Section 193 FA 1994 and  
Section 115(6) FA 1995

para 3, Schedule 21 FA 1995

Section 194 FA 1994 and  
Section 109 FA 1995

para 19, Schedule 19 FA 1994

para 20, Schedule 19 FA 1994

para 21, Schedule 19 FA 1994

para 22, Schedule 19 FA 1994

para 23, Schedule 19 FA 1994  
and Section 110(1) FA 1995

para 41, Schedule 19 FA 1994

para 42, Schedule 19 FA 1994

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## *Introduction*

### **Outline of normal enquiry powers in current system**

- 4.1 Under the current rules the Inland Revenue does not have an explicit right to enquire into a return to ensure it is correct. But the Revenue is required to consider whether a return is correct before making an assessment. If an Inspector is satisfied with the accuracy of the return the assessment must be based on the figures in that return. If the Inspector is not satisfied with the return he may make an assessment, '*to the best of his judgement*', in some other figures (S.29 TMA 1970).
- 4.2 So the Revenue may ask questions of a taxpayer in order to make a judgement on the accuracy of a return. But there are no statutory powers regulating the enquiries that can be made, and no powers requiring the taxpayer to co-operate with the enquiry.
- 4.3 In many cases the enquiry only progresses through the familiar cycle of estimated assessment/taxpayer appeal/Commissioners' hearing. This can be a time consuming process for all concerned and can appear unnecessarily confrontational, particularly when the Revenue is merely seeking to establish the facts of the case.
- 4.4 It is also possible for dishonest taxpayers to arrange their affairs to such a degree that returns appear to be perfectly satisfactory. In many such cases a detailed review of a taxpayer's affairs will quickly establish the true position. But under the current rules the Revenue could not justify opening an enquiry without grounds for dissatisfaction with a return.

### **Outline of enquiry powers under Self Assessment**

- 4.5 Under Self Assessment there will be a completely new approach to the critical examination of returns. This approach will form an integral part of the "process now-check later" regime, and will represent a powerful deterrent to those who do not wish to comply with their tax obligations.
- 4.6 During the routine processing the Revenue will only check the return to the extent of correcting obvious errors (repairs) that have come to light at that stage. For most taxpayers the return, including the self-assessment, will simply be processed as submitted.
- 4.7 Once initial processing has been completed the Inland Revenue will check returns and will have an explicit right to enquire into the completeness and accuracy of *any* tax return. This right will cover all enquiries, from straightforward requests for further information on individual items through to full reviews of books and records. It will be supported by a new information power.
- 4.8 It will not be necessary to justify an enquiry by identifying particular aspects of the return that give cause for concern. So in theory all enquiry cases could be chosen on the basis of a random selection process. Random selection will play an important part in the new regime, but the majority of enquiry cases will continue to be specially selected by reference to the information in the return, and other information in the Revenue's possession, as they are now.
- 4.9 There will be clear rules covering the time limits in which enquiries may be made, the nature of the information that can be sought, and the conduct of the enquiry itself. And at the end of any enquiry the taxpayer will have full rights of appeal if they do not agree with the Revenue's findings. The taxpayer will also have the right to ask the Commissioners to give notice that an enquiry is complete.

- 4.10 The time limit for enquiries only applies to the opening of an enquiry. It does not place any direct constraints on the time taken to complete the enquiry because this will vary according to the nature and complexity of each case. Once the time limit for enquiry has passed the Revenue will not be able to amend a taxpayer's self-assessment and will only be able to make a further (discovery) assessment if the taxpayer has been fraudulent or negligent or has made an incomplete disclosure of information.

#### **Time at which the new enquiry procedures apply**

- 4.11 The new enquiry procedures described in this chapter first apply to the tax returns for 1996/97, the first year of self-assessment.

#### *Power to enquire into returns*

#### **The Revenue will be entitled to enquire into any return**

##### **Section 9A(1)**

- 4.12 Under the new system an officer of the Board will have the right to make enquiries into any return forming the basis of a self-assessment.
- 4.13 This right will apply to the original return, and to any subsequent amendment to the return made by the taxpayer.
- 4.14 It will apply in all cases, including those in which the tax liability is actually calculated by the Revenue. In such cases the Revenue calculation will be made on the basis that the information in the return is correct, but no checks will be made to confirm this *at the time the calculation is made*.

#### **Condition for making enquiry: taxpayer must be notified**

- 4.15 The only condition that the officer of the Board must satisfy before commencing an enquiry is that he must give the taxpayer written notice of his intention to enquire into the return.
- 4.16 If the return is not selected for enquiry within the specified time limits the Revenue will not normally have the right to open an enquiry at any later date. The return and its associated self-assessment will be treated as "final". (But *see para 4.35.*)
- 4.17 The Revenue is under no obligation to give notice that a particular return has been accepted and that no enquiries will be made.

##### **Section 9A(3)**

- 4.18 Only one notice of enquiry may be issued in respect of any return or amendment.

#### **Time limits for notice of enquiry**

##### **Section 9A(2)**

- 4.19 The written notice of enquiry must be issued within a specified period of time following the filing of the return (or the amendment to the return).
- 4.20 Where a return for any tax year is filed (or an amendment is made) on or before the fixed (31 January) filing date for that year, the period in which the notice can be issued will be **the twelve months from the fixed filing date for that year**. This period will end on 30 January following, the day before the fixed filing date for the next return.

- 4.21 If a return for any tax year is filed (or an amendment is made) after the fixed filing date for that year, the period in which the notice can be issued will end on the **quarter date following the anniversary of the actual date of filing of the return or the amendment**. Quarter dates are defined as 31 January, 30 April, 31 July and 31 October.

### *Some notes on Revenue enquiries*

#### **Repairs and enquiries**

- 4.22 The right to “repair” the entries in a return (*para 2.41*) is quite distinct from the right to “enquire” into the accuracy of the information in the return.
- 4.23 A repair is simply the correction of an obvious error in an entry in the return, or the associated computations. In contrast an enquiry may be concerned with the accuracy and technical validity of the entry itself.

#### **Enquiries will comprise a mixture of selected audits and random audits**

- 4.24 Although the Revenue will have the right to check any tax return, at random, including those in which everything appears to be in order, most enquiries will be selective, for example on the basis that there is significant tax at risk, or a suspicion that something is wrong.
- 4.25 In addition to the selective enquiries there will be a smaller number of random selections.
- 4.26 The current Revenue Code of Practice on Investigations requires Inspectors to state their grounds for dissatisfaction with a return before commencing any investigation. This aspect of the Code of Practice will no longer apply under the new regime. However, the Revenue may identify particular areas on which the enquiry will focus, whether the enquiry has been taken up randomly or selectively.

#### **Extent of enquiries**

- 4.27 Some enquiries will simply question obvious errors that were not identified during the initial processing, and some will merely require a straightforward clarification of a single item in the return.
- 4.28 Others will comprise a more detailed examination of some technical aspect of the return, for example, whether a particular expense is allowable for tax purposes. Some large businesses will, as now, be the subject of detailed technical reviews each and every year.
- 4.29 Yet others will have a full in depth review or investigation of the taxpayer’s affairs including the records underlying the entries in the return.
- 4.30 It is impossible to give an indication of the percentage of cases that may be subject to enquiry under the new regime. In many areas where the Revenue currently takes responsibility for assessing income and calculating the tax due the responsibility for doing so will now fall on the taxpayer. So the number of enquiries undertaken will in part depend on how well taxpayers cope with their new responsibilities. In addition a significant proportion of current enquiries relate to the basis of assessment or to matters that are affected by these basis rules. The Revenue expects the number of enquiries on these particular grounds to fall substantially.

- 4.31 The percentage of cases where there is a more detailed examination of some technical aspect of the return or an in depth review or investigation of the taxpayer's affairs is likely to remain small. The Revenue will however monitor compliance levels closely to ensure that taxpayers who do not self-assess correctly face a high risk of being detected and, in the case of negligence or fraud, penalised.

#### **Time limits for commencement of enquiries**

- 4.32 The 12 month time limit before finality is achieved will allow information from third parties - employers, contractors, financial institutions - to be used in the enquiry selection process. It will also allow the Revenue to plan an efficient annual cycle of work.
- 4.33 Whenever a self-assessment is amended by the taxpayer a new period for potential Revenue enquiries begins (i.e. the period given by **Section 9A(2)(b)**). In most cases any subsequent enquiry will be limited to the area of the return that was amended. But there may be cases in which the amendment is so fundamental to the return that the whole return will be considered for enquiry.
- 4.34 For example the original return may have contained an estimated figure. If the correction of the estimate only altered a single entry in the return any subsequent enquiry would normally be limited to that entry. But if that correction altered a number of entries, or radically altered the overall self-assessment, it is possible that the whole return would be considered for enquiry.

#### **Enquiries after time limit for notice of enquiry has elapsed**

- 4.35 It will not be possible for the Revenue to commence enquiries under the new **Section 9A** powers once the time limit for commencing an enquiry has passed. Any enquiries commenced outside these time limits may only be made for the purposes of a discovery assessment under **Section 29** (see *para 4.88 onwards*). In such cases the Revenue will have to rely on the information powers in Sections 20 and 51 TMA 1970 to support the enquiry. Discovery assessments will be limited to where the taxpayer has been fraudulent or negligent, or has failed to disclose all the relevant information.
- 4.36 Where an amendment is required to the liability for an earlier year because of an event in a later year, for instance following a claim to carry back loss relief, the amendment will not re-open that earlier year for enquiry (in this context see *para 6.26*)

### *Enquiry Procedures*

#### **The new procedures apply to any formal enquiry made under Section 9A(1)**

##### **Section 19A(1) & (2)**

- 4.37 The new procedures only apply where an officer of the Board has issued a formal notice of enquiry in respect of any return, or an amendment to a return.
- 4.38 The general information powers of S.20 TMA 1970 (which apply to both taxpayers and third parties) and S.51 TMA 1970 (Commissioners' right to issue precept for information) will continue to apply where appropriate.
- 4.39 Although there are some apparent similarities between **Section 19A** and S.20 TMA 1970 they fulfil two distinct and separate functions.

- 4.40 **Section 19A** provides part of the formal framework for the “check later” component of “process now - check later”. As such it will only apply where an officer of the Board is seeking to establish the accuracy of a particular return. And there will be a fixed time limit in which the enquiry can be started. The information that can be sought is limited to that which is reasonably relevant to determining whether or not the return is correct.
- 4.41 By contrast S.20 TMA 1970 is a general investigative power, which can be used in a wide variety of circumstances. It allows the officer to seek information relating to any tax liability to which the taxpayer may or may not be subject. It is not restricted to a particular return, or to a particular period. And it can be used to obtain information from third parties.

### **Formal notice may be given requesting documents, accounts or particulars**

#### **Section 19A(2)**

- 4.42 The officer of the Board making the enquiry may also issue a notice requiring the production of documents, accounts or other written particulars. This notice may be issued at the same time as the notice of enquiry, or at some later date.

### **The taxpayer must be given at least 30 days to comply with the request**

- 4.43 Whenever a formal notice is issued that notice must specify a time limit for compliance with the notice. This time limit must be not less than 30 days.
- 4.44 If taxpayers require a longer period to provide the information requested they should contact the officer to explain the problem. In genuine cases a revised time scale will be agreed.
- 4.45 Where, exceptionally, the taxpayer cannot obtain the information, or it does not exist, the taxpayer should explain the circumstances to the officer dealing with the enquiry.

### **Limits on the information and documents that may be requested**

#### **Section 19A(2)(a)**

- 4.46 The officer may only request documents that are in the taxpayer’s possession or power. And those documents must be documents which, in the officer’s reasonable opinion, are required to determine
- whether or not a particular return is incomplete
  - whether or not a particular return or amendment is incorrect.

#### **Section 19A(2)(b)**

- 4.47 In addition to any documents the officer may request any “accounts or particulars” which are required to determine the accuracy or completeness of any return.
- 4.48 The word “particulars” is used in the ordinary sense of “detailed account”. So, for example, the taxpayer may be asked to give a detailed factual account of how an entry in a return is made up.
- 4.49 The rules in **Section 19A** only apply to written requests for written information. The officer has no power to require someone to attend an interview. But of course a meeting will often be a more effective way of resolving an enquiry.

### ***Section 19A(5)***

4.50 The taxpayer does not have to supply any documents, accounts or particulars relating to the conduct of any pending appeal.

### **Nature and amount of information that may be requested**

4.51 Clearly the nature and quantity of documents etc. that will be requested in any case will depend on the nature of the enquiry. But in all cases the request must be limited to documents etc. connected with the return.

4.52 For example, for a simple technical enquiry into expenditure qualifying for capital allowances the request would be limited to the documents etc. detailing that expenditure. But for a full in depth review of a business the request would cover all the records of that business.

4.53 Information such as details of a taxpayer's personal expenditure, personal assets or non taxable income may be required during an investigation. Unless such information can be shown to be reasonably relevant to an entry in the return it can not be requested under ***Section 19A***. But as now any such information can be sought informally, and if not provided informally, it can be sought formally under S.20 TMA 1970.

4.54 Unlike S.20 there is no restriction on the information that can be requested from a barrister, advocate or solicitor. This is because the request for information is already limited to information that can be shown to be reasonably relevant to an entry in the taxpayer's personal tax return.

### **Compliance with request for documents or information**

#### ***Section 19A(3)***

4.55 The taxpayer may provide copies of documents instead of the originals. But the officer has the right to give formal notice that the original documents are required for inspection.

#### ***Section 19A(4)***

4.56 The officer also has the right to take copies of, or make extracts from, any document produced.

### **Appeals against requests for documents, accounts or particulars**

#### ***Section 19A(6) to (11)***

4.57 The taxpayer may appeal against the formal notice requesting documents, accounts or particulars. Any appeal must be made within 30 days of the date on which the notice requesting the documents is given.

4.58 There are no conditions limiting the terms of the appeal. But the potential grounds for any such appeal are limited because the only points open to arbitration are

- whether the information requested is reasonably relevant to determining whether or not a return is complete and correct, and
- whether the taxpayer has been given sufficient time to comply with the notice.

The appeal cannot be used to challenge the Revenue's right to make enquiries into any return.

- 4.59 The normal appeal procedures (as set out for assessments) will apply to any such appeal.
- 4.60 When determining the appeal the Commissioners will either
- confirm the original notice, or
  - confirm only that part of the notice which they consider to be reasonably required to determine the accuracy and completeness of any return or amendment, or
  - set the notice aside.
- 4.61 Whenever a notice is confirmed that notice must be complied with within 30 days of the determination of the appeal.
- 4.62 Neither party will be entitled to require a stated case. This is because it is a question of fact whether or not the information requested is reasonably relevant to determine the accuracy of the return.

### **Failure to comply with a notice requesting documents accounts or particulars**

#### ***Section 97AA***

- 4.63 Failure to comply with a document request notice may result in the determination of a penalty.

#### ***Section 97AA(1)***

- 4.64 The initial penalty will be £50. But if the failure continues after the determination of the penalty additional daily penalties may be imposed.

#### ***Section 97AA(2) & (3)***

- 4.65 If the additional daily penalty is determined by an authorised officer of the Board (***Section 100***) the maximum penalty that can be imposed is £30 per day. But if the penalty is determined by the Commissioners in formal penalty proceedings (***Section 100C***) the maximum is £150 per day.

- 4.66 The taxpayer can appeal against the penalty in the normal way (***Section 100B***).

#### ***Section 97AA(4)***

- 4.67 No penalty can be determined after the failure has been corrected.
- 4.68 There can be no question of a penalty in any case in which it is genuinely impossible, for whatever reason, to comply with the notice.
- 4.69 A taxpayer cannot be penalised for failing to produce records that do not exist. So whenever the taxpayer has failed to keep the records required by ***Section 12B*** a penalty may arise for that failure, but not for any consequential failure under ***Section 19A***.
- 4.70 However, where, exceptionally, the taxpayer has kept *some* records, but fails to comply with a request to produce them, penalties could be sought for both the failure under ***Section 12B*** and the failure under ***Section 19A***.

## *Settlement of an enquiry*

### **Officer of the Board will issue a formal notice stating that an enquiry is complete**

#### ***Section 28A(1) & (5)***

4.71 Any formal enquiry made under **Section 9A** will be treated as completed when an officer of the Board issues the taxpayer with a notice to that effect. The notice will state the officer's conclusions regarding any adjustments that are required to the self-assessment associated with the return that had been under enquiry.

### **The self-assessment will then be amended by the taxpayer**

#### ***Section 28A(3)***

4.72 Once the completion of enquiry notice has been issued the taxpayer has 30 days in which to amend the self-assessment. The extent to which the self-assessment can be amended depends on the time at which the return was submitted.

#### ***Section 28A(3)(a)***

4.73 In all cases the taxpayer may make any amendments required to take into account the adjustments arising from the enquiry.

#### ***Section 28A(3)(b)***

4.74 Additional amendments may be made by any taxpayer when

- the enquiry related to a return (rather than an amendment to a return) and
- that return was submitted on or before the normal filing date for that return, or during the following 12 months (the normal period in which taxpayer amendments can be made: *para 2.42*) .

In such cases the taxpayer may make any other amendment to the return providing that amendment is notified to the officer.

4.75 This facility to make further amendments is provided in case the taxpayer wishes, for example, to revise any previous claim, or make any supplementary claim, following the outcome of the enquiry.

### **Further amendment by the officer of the Board**

#### ***Section 28A(4)***

4.76 Where the officer of the Board believes that the amended self-assessment prepared by the taxpayer is incorrect the officer may further amend the self-assessment.

4.77 Any such further amendment must be made by formal notification to the taxpayer within the 30 days following the expiry of the 30 day time limit for taxpayer amendments. This amendment may be the subject of an appeal.

4.78 Where the enquiry related only to an amendment any further amendment must similarly be restricted to that aspect of the return.

## **Amendments during the course of an enquiry**

### **Section 28A(2)**

- 4.79 It may be that during the course of an enquiry an officer of the Board has reason to believe that there is likely to be a loss of tax unless the self-assessment is increased immediately. For example, omissions of taxable items may have been established but the taxpayer has refused to make a payment on account of the final settlement, or the officer may have information to suggest that the taxpayer is planning to remove assets abroad.
- 4.80 In any such case the officer of the Board may issue a notice amending the self-assessment accordingly.

## **Application for direction that the enquiry is complete**

### **Section 28A(6) & (7)**

- 4.81 During the course of an enquiry the taxpayer may consider that the officer of the Board has no reasonable grounds for continuing the enquiry, and that therefore the enquiry should be concluded.
- 4.82 In any such case the taxpayer may apply to the Commissioners seeking that a notice be issued stating that the enquiry is complete. This application will be determined as if it were an appeal.
- 4.83 This right to apply to the Commissioners does not restrict the Revenue's right to make an enquiry into any return. But if the taxpayer has provided the Revenue with all the information reasonably required to determine the accuracy or completeness of the return, it allows the taxpayer to ensure that the enquiry is not unreasonably prolonged.

## **Appeals against Revenue amendments**

### **Section 31(1)(a)**

- 4.84 The taxpayer has the right of appeal against any amendment made by the Revenue under **Section 28A(2)** or (4). Any appeal must be made in writing within 30 days of the date on which the amendment was issued. And the normal procedures for appeals, and postponement applications, will apply.

### **Section 31(1A)**

- 4.85 But where the appeal is made under **Section 28A(2)** the appeal will not be heard or determined until the officer has completed the enquiries.

## **Settlement of enquiries by agreement, including contract settlements**

- 4.86 The formal procedures for settling enquiries (*paras 4.71 to 4.85*) ensure that the taxpayer and the Revenue have equal rights to put their case, if necessary, before the Commissioners. It is expected however that in the vast majority of cases settlement will be by agreement and by an amendment to the self-assessment to reflect any adjustments agreed. The facility to agree a contract settlement for all outstanding items will remain broadly as now.

## *Penalties for incorrect returns*

### **Existing penalties will continue to apply**

#### *Section 95*

- 4.87 The existing rules for penalties following the fraudulent or negligent filing of an incorrect return will continue to apply in respect of all self-assessment returns (*see also paras 2.60 and 2.61*).

## *Discovery assessments*

### **The only assessments issued by the Revenue in self-assessment cases will be discovery assessments**

#### *Section 29*

- 4.88 Self-assessments will replace the vast majority of estimated or agreed figure assessments currently issued by the Revenue (under S.29(1) TMA 1970). But the Revenue will still require the power to make “discovery assessments”, that is assessments currently made under S.29(3) TMA 1970 to prevent a loss of tax.
- 4.89 S.29 TMA 1970 has been recast to provide general rules for Revenue assessments to prevent any loss of tax. But the new rules limit the right to make a discovery assessment for any period if a self-assessment has already been made by the taxpayer for that period.
- 4.90 The rules that apply where a self-assessment has already been made embody the principles established in case law, and in particular in the case of *Scorer v Olin Energy Systems Limited* [58 TC p592]. In cases not involving fraud or negligence they provide that if the information “discovered” was already in the Revenue’s possession when the self-assessment became final, the Revenue will have no right to make a discovery assessment.
- 4.91 These rules ensure that a taxpayer who has made a full disclosure in the return will have absolute finality 12 months after the filing date. This will be the case even if the return is subsequently found to be incorrect, *unless* it was incorrect because of fraudulent or negligent conduct. In any case where there was incomplete disclosure or fraudulent or negligent conduct the Revenue will still have the power to remedy any loss of tax.

### **General circumstances in which discovery assessments can be made**

#### *Section 29(1)*

- 4.92 Subject to the conditions considered below an officer of the Board (or the Board itself) will be able to make a discovery assessment for a tax year if it is discovered that
- there are profits which ought to have been assessed but have not been assessed, or
  - an assessment (including any self-assessment) is, or has become insufficient, or
  - any relief that has been given is, or has become excessive.
- 4.93 The assessment will be in the amount (or the further amount) which the officer (or the Board) believes will make good to the Crown the loss of tax.

### ***Section 30(1B)***

4.94 An officer of the Board may also make a discovery assessment to recover any repayment of tax that should not have been made.

### **Restrictions on right to make discovery assessments where a self-assessment has already been made for the relevant period**

#### ***Section 29(2)***

4.95 In any case in which a self-assessment has already been made for the relevant period a discovery assessment will not be made where

- the loss of tax arose out of an error or mistake concerning the basis on which the returned tax liability was calculated, and
- that basis was the generally prevailing practice at the time the return was made.

4.96 So the Revenue will not be able to raise discovery assessments simply because it has changed its practice in relation to the treatment of some particular item.

#### ***Section 29(3) to (5)***

4.97 In the case of any self-assessment a discovery assessment cannot be made unless either

- the loss of tax is the result of fraudulent or negligent conduct by the taxpayer or any person acting on the taxpayer's behalf, or
- the officer could not have been reasonably expected to have identified the circumstances giving rise to the loss of tax, before the expiry of the normal enquiry period, or before the conclusion of any enquiry, using the information that had then been "*made available*".

#### **Definition of "*made available*"**

#### ***Section 29(6) & (7)***

4.98 Information will be treated as having been made available to the officer if

- it is contained in the return for the relevant period (or the two preceding periods) or in any of the accounts, statements or documents supplied with the return, or
- it is contained in any claim made for the relevant period (or the two preceding periods), or in any of the accounts, statements or documents supplied with the claim, or
- it is contained in any documents, accounts or particulars supplied in connection with an enquiry into a return or claim, or
- it is information which could reasonably be expected to be inferred from any of the above, or
- it is information that was notified to the officer in writing by the taxpayer.

4.99 So a change of opinion on information that has previously been made available to the Revenue will not be grounds for a discovery.

4.100 The definitions of “made available” must be considered in the context of the “reasonably expected” condition of **Section 29(5)**. There is clearly an onus on the taxpayer to draw attention to any important information relevant to a tax liability, particularly if there is some doubt as to the interpretation that can be placed on that information. It is not sufficient just to provide that information if it is hidden away or obscure.

### *Procedures for making Revenue assessments*

#### **Section 30A**

4.101 The procedures for making Revenue assessments are essentially those that apply now (S.29(1) and (4) to (7) TMA 1970). These can now be found in **Section 30A**.

### *Time limits for discovery assessments*

#### **Section 34(1)**

4.102 In any case of incomplete disclosure without fraudulent or negligent conduct the time limit for a discovery assessment will be 5 years from 31 January next following the tax year to which it relates.

#### **Section 36(1)**

4.103 In any case with fraudulent or negligent conduct the time limit for a discovery assessment will be 20 years from 31 January next following the tax year to which it relates.

### **Payment of tax**

#### **Section 59B(6)**

4.104 The due date for tax charged by a discovery assessment is 30 days after the notice of the assessment.

### *Appeals*

#### **Existing procedures to apply**

4.105 The normal appeal procedures will apply in respect of any appeal against a Revenue assessment (e.g. **Sections 31, 50, 55** etc.).

#### **Appeals that relevant conditions for discovery assessment do not apply**

#### **Section 29(8)**

4.106 Any objection that the conditions at **Section 29(4)** or **(5)** do not apply must be made by an appeal against the assessment.

### *Interest, surcharges and penalties*

4.107 Interest will be due, from the due date for the relevant tax year, and either surcharge or penalties may be sought in respect of the tax charged in a discovery assessment.

## *Conversion table*

### **TMA 1970**

***Section 9A***

***Section 19A***

***Section 28A***

***Section 29***

***Section 30(1B)***

***Section 30A***

***Section 31(1)-(3)***

***Section 34(1)***

***Section 36(1)***

***Section 59B***

***Section 97AA***

***Section 98B2***

***Section 100B(1) & (2)***

***Section 103A***

as inserted by

as inserted by

as inserted by

as substituted by

as inserted by

as inserted by

as substituted by

as amended by

as amended by

as inserted by

as inserted by

as amended by

as amended by

as amended by

### **FA 94 and FA 95**

Section 180 FA 1994

Section 187 FA 1994

Section 188 FA 1994

Section 191 FA 1994

para 4, Schedule 19 FA 1994

para 5, Schedule 19 FA 1994

para 7, Schedule 19 FA 1994

para 10, Schedule 19 FA 1994

para 11, Schedule 19 FA 1994

Section 193 FA 1994 and

Section 115(6) FA 1995

para 29, Schedule 19 FA 1994

para 30, Schedule 19 FA 1994

para 31, Schedule 19 FA 1994

and Section 115(7) FA 1995

para 33, Schedule 19 FA 1994

and Section 115(8) FA 1995

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## *Introduction*

### **There will be no partnership assessments under Self Assessment**

- 5.1 Under the existing rules the profits of a Case I/II business carried on in partnership are taxed by making an assessment on the partnership (S.111 ICTA 1988).
- 5.2 This assessment is a composite assessment taking into account the tax rates, personal reliefs and allowances appropriate to the individual partners making up the partnership (S.277 ICTA 1988). But it is the partnership that is liable for the tax due.
- 5.3 The rules for returning the information required to make the partnership assessment, and for the collection of tax, are identical to those that apply for individuals. But in all cases it is the partnership that is required to take the appropriate action rather than the individual partners. So, for example, the partnership is required to file a partnership return (S.9 TMA 1970).
- 5.4 There will be no partnership assessments under Self Assessment. Instead each partner will be assessed on his or her share of the partnership profits, and each partner will be solely responsible for the tax due on that share. So individual partners will be required to include their share of any partnership profits in their own return of total income, and in their own self-assessment.

### **But a partnership return will be required to allow partnership matters to be dealt with centrally**

- 5.5 The rules for calculating taxable profits operate by reference to sources of income. Where, for example, a partnership carries on a trade, that trade is a single source within Case I Schedule D regardless of the number of partners entitled to share the profits from that trade.
- 5.6 So although the rules for the assessment and collection of tax will operate on the partners as if the partnership did not exist, it makes practical sense for both taxpayers and the Revenue if all matters relating to the calculation of partnership profits, income or gains are dealt with centrally in a partnership return made by the partnership on behalf of all the partners.
- 5.7 The partnership return will include all information required to calculate the profits arising from any partnership business in the accounting periods covered by the return, including any claims (such as capital allowances) that must be taken into account when calculating the profits of that trade. In addition it will include details of any partnership investment income.
- 5.8 The partnership return will also need to include details of the profit allocation in force for the accounting periods covered by the return.
- 5.9 The partnership return will be subject to the same Self Assessment enquiry procedures that will apply to individual returns.
- 5.10 Individual partners will not be entitled to make any adjustments to the amount of partnership profit allocated to them in the partnership return. They will be required to include exactly the same figure of their share of the partnership profit in their personal return of total income.

## Time at which the new rules will apply for partnerships

### *Section 199 FA 1994 (Section 215(4) & (5) FA 1994)*

- 5.11 1996/97 is the first year of Self Assessment for personal returns, including returns completed by individual partners. This will also be the first year in which the new Self Assessment partnership returns will be required.
- 5.12 A Self Assessment partnership return **will be required from all partnerships for 1996/97**. But there will still be composite partnership assessments for 1996/97 for any partnership set up and commenced on or before 5 April 1994 for which
- there have been no changes in the composition of the partnership in the period 6/4/94 to 5/4/97, or
  - there have been changes in the composition of the partnership in the period 6/4/94 to 5/4/97, but a continuation election was made (under S.113(2) ICTA 1988) in respect of each such change.

For any such partnership the new rules for separate assessment of individual partners will first apply in the following year, 1997/98.

- 5.13 For any partnership set up and commenced (or deemed to have commenced) on or after 6 April 1994 the new rules for separate assessment of individual partners will apply **from the date of commencement (Section 111 ICTA 1988)**.

## *Partnership returns*

### **A partnership return will be required to aid assessment of the individual partners**

#### *Section 12AA(1)*

- 5.14 All partnerships will be required to complete and file a partnership return to aid the assessment of the members of the partnership, including any corporate members.

As with individuals the return will require a return of the partnership's 'total income'. The amounts returned should be the *net* amounts of any taxable income, after taking into account any relief, allowance or repayment for which a claim is made by the partnership. A return will also be required of any tax credits arising on partnership income.

## Information required in the return

### *Section 12AA(2) & (3)*

- 5.15 The return will be issued to the partnership with a notice requiring the partner identified in accordance with that notice to complete the return. That partner will be responsible for filing the information, accounts, statements and documents that may reasonably be required by an officer of the Board for "*such period as may be specified in the return*". In default the Revenue may identify any other partner to complete the return.
- 5.16 The period covered by the return may vary according to whether the partnership is a partnership of individuals, or whether it includes one or more companies. For example, for individuals the partnership return will require a return of information for all accounting periods ending in a particular tax year.

- 5.17 Partnerships may choose to nominate one particular partner to receive and complete the partnership returns.

#### **Time limits for filing of the return must accommodate both individuals and companies**

- 5.18 The filing dates for a completed return must accommodate both individual and corporate partners.

#### **Time limits for individuals**

##### ***Section 12AA(4)***

- 5.19 Where the completed return is required in connection with one or more individuals the filing date for the return will not be earlier than the appropriate filing date for those individuals.
- 5.20 So where the return is issued at the normal time the filing date will be 31 January following the relevant tax year. Where the return is issued late (that is after 31 October following the relevant tax year) the filing date will be 3 months after the date of issue of the return.

#### **Time limits for corporate partners**

##### ***Section 12AA(5)***

- 5.21 Where the completed return is required in connection with one or more companies the filing date for the return will be set by reference to the period covered by the return.
- 5.22 So where the return was issued at the normal time the filing date will be not earlier than 12 months from the end of the period covered by the return. Where the return was issued late (that is more than 9 months after the end of the relevant period) the filing date will be 3 months after the date of issue of the return.

#### **Time limits for mixed partnerships**

- 5.23 The time limits for the filing of the partnership return have to be flexible enough to cope with the different types of partnership, and hence combinations of filing dates, that can exist.

Where the accounting date of a mixed partnership falls on or between 6 April and 31 January in any tax year the filing date for the partnership return will be the **31 January next following the tax year**. For any such case the 31 January filing date satisfies both ***Section 12AA(4)(a)*** (for individuals) and ***Section 12AA(5)(a)*** (for corporate partners).

But where the accounting date of a mixed partnership falls on or between 1 February and 5 April in any tax year the filing date for the partnership return will be the **first anniversary of that accounting date**. Again this rule ensures that both ***Section 12AA(4)(a)*** (for individuals) and ***Section 12AA(5)(a)*** (for corporate partners) are satisfied.

Where the accounting date of a mixed partnership falls on or between 1 February and 5 April in any tax year any members of the partnership who are individuals will be required to file their own personal returns before the partnership return is required.

- 5.24 In such cases it may be that the partnership return can be completed and submitted before the formal filing date. But where this is not possible the partner will have to include an estimate of his or her share of partnership profits in the return, and then correct it when the final figure becomes available.

## **Details of partners must be included in the return**

### ***Section 12AA(6) & (10)***

- 5.25 The return must include the names, addresses (or registered office) and tax references of each of the partners in the partnership. It must also include a declaration by the person making the return that to the best of that person's knowledge and belief the return is correct and complete.
- 5.26 The identification of individual partners will allow the partnership return to be cross checked against individual returns.

## **Details relating to the disposal of partnership property must be included in the return**

### ***Section 12AA(7)***

- 5.27 The return should include any details required to calculate chargeable gains arising on partnership assets, for example the disposal proceeds. And, if required, the return should include details of any assets acquired by the partnership.
- 5.28 But the partnership will not be required to provide capital gains tax computations. This is because there will have to be a separate calculation for each partner to take into account different periods of ownership and different acquisition values.

## **More than one tax computation may be required**

### ***Section 12AA(9)***

- 5.29 The information in the return may require different information, accounts and statements for different types of partnership.
- 5.30 For example, where a partnership includes both individuals and companies at least two free standing profit calculations will be required with the return. One calculation will use income tax rules, as if the partnership profits arose solely to individuals, and appropriate profit shares will be allocated to all those members liable to income tax. The second will use corporation tax rules, as if the partnership profits arose to a company, and appropriate profit shares will be allocated to all those members liable to corporation tax.

## **Claims and elections**

### ***Section 42(6) & (7)***

- 5.31 Certain specified claims and elections must be made in the partnership return. These are those claims and elections that have a bearing on the computation of partnership profit, for example claims to capital allowances and to relief for pre-trading expenditure.

## *Partnership statements*

### **Partnership returns will include a “partnership statement”**

#### ***Section 12AB(1)***

5.32 As there will no longer be any partnership assessments the partnership return will not have to include any self-assessment. But instead the return will have to include a “partnership statement”. This statement will be a statement of

- the total income, losses, tax credits and charges of the partnership for each period of account ending in the return period, and
- each partner’s share of that income, loss, tax credit or charge.

### **The partnership statement will be subject to repair by the Revenue and amendment by the taxpayer**

#### ***Section 12AB(2) & (3)***

5.33 The partnership statement will be subject to the same rules regarding repair by an officer of the Board, or amendment by the partnership, as a self-assessment.

5.34 An officer of the Board may amend a partnership statement to correct any obvious errors or mistakes in the return providing any such repair is made within 9 months of the date on which the completed return is filed with the Revenue.

5.35 The partnership may amend the partnership statement to give effect to any amendment to the information in the return providing any such amendment is made within 12 months of the filing date for that return. But this right to amend the partnership statement is suspended during any period in which the return is under enquiry. (The partnership will have the right to make appropriate amendments once the enquiry is complete.)

### **Error or mistake relief**

#### ***Section 33A***

5.36 The partnership will also have the right to make an error or mistake relief claim in respect of the partnership statement at a later date. Any such claim must be made within 5 years of the annual filing date for the return.

### **Any repairs or amendments will give rise to adjustments to the partners’ self-assessments**

#### ***Section 12AB(4)***

5.37 Where a partnership statement is repaired by an officer of the Board, or amended by the partnership, corresponding changes must be made to the individual partners’ self-assessments.

5.38 In either case notices will be issued to each partner by the Revenue amending any self-assessment previously returned.

## *Requirement to keep records on which partnership return is based*

### **Partnerships will be required to make and keep documents**

#### ***Section 12B***

5.39 The rules for the making and keeping of documents apply in respect of partnership returns as they apply to self-assessment returns (*see paras 2.98 to 2.111*).

## *Sanctions against failure to file a return*

### **Penalties for failure to file a partnership return on time**

#### ***Section 93A(1)***

5.40 As with personal returns there will be both fixed and daily penalties for a failure to file a partnership return. If the time limits for filing of the return are not met fixed penalties will automatically arise. And in more substantial cases additional daily penalties may be sought.

### **Fixed penalties**

#### ***Section 93A(2)***

5.41 The initial penalty will be fixed at £100 for each partner who was a member of the partnership during the period covered by the return and will be charged on individual partners not the partnership. This penalty will apply if the partnership return is not filed on the date specified in the return (the filing date).

#### ***Section 93A(4)***

5.42 If the return is still outstanding 6 months after the filing date there will be a further penalty of £100 per partner unless an officer of the Board has already applied to the Commissioners for a daily penalty.

5.43 Both these fixed penalties will be determined by an officer of the Board (*Section 100*). There is no provision for these fixed penalties to be restricted where the tax due on partnership profits is minimal.

### **Appeals against the determination of a fixed penalty**

#### ***Section 93A(6) & (7)***

5.44 Any appeal against the determination of a fixed penalty must be made by the representative partner on behalf of all the partners concerned. Any such appeal will be treated as a composite appeal against each individual penalty, and the representative partner will be treated as if he or she were the partner liable to each penalty.

5.45 The Commissioners can only set the penalty aside if the representative partner had a reasonable excuse for the failure that occurred during the period between the filing date and the submission of the partnership return. Any such reasonable excuse must apply for the whole period of delay. It will not be sufficient for there to have been a reasonable excuse for part of the period.

## Daily penalties in more substantial cases

### *Section 93A(3)*

5.46 In addition to the fixed penalties a daily penalty of up to £60 per relevant partner, per day, may be imposed if leave is given by the Commissioners (although if any such penalty is applied for within 6 months of the filing date the second fixed penalty no longer applies).

5.47 The daily penalties apply for each day on which the failure continues following issue of the notice of the direction by the Commissioners that they are to apply. **Again the penalties will be charged on individual partners not the partnership.**

### *Section 93A(5)*

5.48 No daily penalty can be imposed once the return has been filed.

## Appeals against daily penalties

### *Section 93A(6)*

5.49 The partnership will have the normal right of appeal against the determination of a daily penalty. But again any such appeal must be made by the representative partner, and will be treated as a composite appeal made on behalf of all the relevant partners.

## Tax geared penalties can only be determined on individual partners

5.50 Where a partner fails to file a personal return on time, and the partnership return is also late, that partner will be liable to 2 sets of fixed penalties. But there is no tax-geared penalty within *Section 93A* because the partnership is no longer liable for any of the tax on partnership profits. Where an individual partner's return is late the tax on the partner's share of the partnership income will be included in the calculation of any penalty chargeable on the partner under *Section 93(5)* (see para 2.77).

## *Enquiries into partnership returns*

### **The Self Assessment enquiry procedures will apply to partnership statements**

#### *Section 12AC*

5.51 Partnership statements will be subject to precisely the same enquiry procedures as individual returns.

#### *Section 12AC(1)*

5.52 An officer of the Board will be entitled to enquire into the accuracy and completeness of any partnership statement, or amendment to such statement, providing the officer notifies the partnership of the intention to do so.

#### *Section 12AC(2) & (4)*

5.53 The enquiry must normally be made within 12 months of the normal filing date. But if the return (or amendment) was filed after the normal filing date, the enquiry period ends with the first quarter date falling 12 months or more after the date of filing.

5.54 Enquiries can be commenced only once in respect of any particular return or amendment (under this section).

## **Any enquiry into a partnership statement will automatically extend to the partners' own returns**

### ***Section 12AC(3)***

- 5.55 A notice of enquiry into a partnership statement will be treated as including a notice of enquiry to each of the members of that partnership who have filed their own personal returns. The Revenue will endeavour to notify each partner when an enquiry on the partnership is commenced.

In the case of a mixed partnership of individuals and companies ***Section 12AC(3)*** ensures that the partner's return is deemed to be under enquiry even though the time limit for a commencing an enquiry under Section 9A or 11AB may have passed.

- 5.56 The purpose of this section is simply to allow the Revenue to make any adjustments to the self-assessments of individual partners following an enquiry into the partnership statement. All the partners' returns will remain open until the partnership enquiry is complete.

This section does not mean that other (non-partnership) aspects of a partner's return are automatically under enquiry. The non-partnership aspects of a partner's return can only be reviewed if a **separate enquiry** is opened under ***Section 9A*** (or, where the time limit for such a notice has passed, if the 'discovery' rules apply). Similarly, the completion of an enquiry into one part of the return (for example, the partnership income) has no consequence for any separate enquiry into the other part (the non-partnership income).

- 5.57 An enquiry into an individual partner's return does not automatically open up the partnership statement for enquiry.

## **Any matters relating to the enquiry will be dealt with through a nominated partner**

### ***Section 12AC(6)***

- 5.58 The partner nominated to file the partnership return and partnership statement will normally be responsible for dealing with any enquiry. But where that partner is no longer available, for example because of retirement, a different partner may be nominated as the successor.
- 5.59 The nominated partner will be responsible for keeping the other partners informed of the progress of the enquiry.

## *Power to call for documents*

### **The new formal procedures also apply to partnerships**

#### ***Section 19A***

- 5.60 The Revenue will have the same rights to call for partnership documents for enquiry purposes as it has for individuals (*see paras 4.37 to 4.62*).

#### ***Section 97AA***

- 5.61 And the same penalties will apply for any failure to file documents required under ***Section 19A*** (*see paras 4.63 to 4.70*).

## *Settlement of an enquiry*

### **Section 28B**

5.62 The rules for the conduct of an enquiry, and for amending a partnership statement following an enquiry, mirror those for amending a self-assessment. They also provide for the corresponding amendments to each partner's self-assessment.

### **Officer of the Board will issue a formal completion of enquiry notice**

#### ***Section 28B(1) & (5)***

5.63 Any formal enquiry into a return, or an amendment of a return, under **Section 12AC** will be treated as complete when an officer of the Board issues the representative partner with a notice to that effect. The notice will state the officer's conclusions regarding any adjustment that is required to the partnership statement.

### **The partnership statement may then be amended by the representative partner**

#### ***Section 28B(2)(a)***

5.64 The representative partner may amend the partnership statement in the 30 days following notification that the enquiry is complete to give effect to adjustments arising from the enquiry.

#### ***Section 28B(2)(b)***

5.65 Additional amendments may be made in any case in which the enquiry related to a return submitted on or before the normal filing date for that return, or during the following 12 months (the normal period in which amendments can be made if the return is filed on time).

### **Further amendment by the officer of the Board**

#### ***Section 28B(3)***

5.66 Where the officer of the Board believes the statement is still incorrect (either because of changes made to the original statement under **Section 28B(2)**, or because no changes have been made to the original statement) the officer may make further amendments to the partnership statement.

5.67 Any such further amendment must be made by formal notification to the representative partner within the 30 days following the expiry of the 30 day time limit for amendments on behalf of the partnership.

### **Right of appeal against Revenue amendment**

#### ***Section 31(1)(b)***

5.68 The representative partner has the right of appeal against any further amendment of the partnership statement under **Section 28B(3)**.

## **Application for direction that completion of enquiry notice be issued**

### ***Section 28B(6)***

5.69 The representative partner may apply to the Commissioners to direct that the enquiry is complete if it is believed that the officer has no grounds for prolonging it.

## **Notice to amend each partner's self-assessment**

### ***Section 28B(4)***

5.70 Individual partners have no right of appeal to the Commissioner in respect of the corresponding amendments to their self-assessments. Instead those corresponding amendments will only be made once the partnership statement has been finalised, whether by agreement with the officer of the Board, or following an appeal to the Commissioners.

5.71 The officer of the Board is required both to notify all the individual partners of the amendments required to their individual self-assessments, and to make those amendments.

## **Discovery and partnerships**

### ***Section 30B***

5.72 Although discovery assessments must be made on individual partners there are specific discovery rules in respect of the partnership statement itself.

### ***Section 30B(1)***

5.73 An officer of the Board may amend a partnership statement where the officer discovers that

- profits have been omitted from the statement
- the profits included are, or have become, insufficient
- the reliefs or allowances claimed in the statement are, or have become, excessive.

### ***Section 31(1)***

5.74 The representative partner has the right of appeal against any such amendment.

### ***Section 30B(2)***

5.75 Where a discovery amendment is made the officer may also make the corresponding amendments to the partners' individual self-assessments, but only once the partnership statement is finalised.

### ***Section 29 and Section 36(1)***

5.76 Alternatively individual discovery assessments may be required. If so the normal time limits for discovery assessments apply.

### ***Section 30B(3) to (10)***

- 5.77 The conditions under which discovery amendments may be made mirror those for discovery assessments (*see paras 4.88 to 4.100*). So, for example, there must have been incomplete disclosure or fraudulent or negligent conduct by one of the partners, or a person acting on behalf of that partner.
- 5.78 Similarly, there can be no discovery simply because of a change in Revenue practice at a later date.

### **Penalties for an incorrect partnership return**

#### ***Section 95A***

5.79 Where the representative partner submits

- an incorrect partnership return, or
- incorrect accounts connected with that return, or
- an incorrect statement or declaration connected with that return,

and does so fraudulently or negligently, or as a result of fraudulent or negligent conduct by any other member of the partnership during the period covered by the return, each member of the partnership will be liable to a tax geared penalty. Any such penalty will be computed on an individual basis, by reference to the additional tax that each individual partner is required to pay as a result of that offence.

#### ***Section 95A(3)***

5.80 Where two or more partners wish to appeal against the determination of a penalty they must do so through the representative partner. An appeal made by the representative partner will be a composite appeal against the determination of each penalty.

### ***Responsibilities of individual partners***

- 5.81 Under Self Assessment each partner will be responsible for paying the tax due on his or her own share of the partnership profits and gains. This tax will be computed in a self-assessment in the normal way.
- 5.82 Because each partner is individually responsible for their own tax it is possible for one partner to settle his or her own tax affairs even though a fellow partner has failed to file a return, or has a return under enquiry for reasons completely unconnected with the partnership (*but see para 5.56*).
- 5.83 Equally there will no longer be joint liability for the tax due on partnership profits. If a particular partner fails to pay the tax due on a share of partnership profits the Revenue will only be able to take sanctions (and ultimately recovery proceedings) against that partner, and that partner alone.

## *Conversion table*

### **TMA 1970**

#### ***Section 12AA***

as inserted by

#### ***Section 12AB***

as inserted by

#### ***Section 12AC***

as inserted by

#### ***Section 28B***

as inserted by

#### ***Section 30B***

as inserted by

#### ***Section 33A***

as inserted by

#### ***Section 93A***

as inserted by

#### ***Section 95A***

as inserted by

#### ***Section 97AA***

as inserted by

### **FA 94 and FA 95**

Section 184 FA 1994 and Sections  
104(6) and 115(4) FA 1995

Section 185 FA 1994 and Section  
104(7) and (8) FA 1995

Section 186 FA 1994

Section 189 FA 1994

para 6, Schedule 19 FA 1994 and  
Section 115(5) FA 1995

para 9, Schedule 19 FA 1994

para 26, Schedule 19 FA 1994

para 28, Schedule 19 FA 1994

para 29, Schedule 19 FA 1994

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## Introduction

### Claims, elections and notices in the existing regime

- 6.1 There are currently some 500 different claims, elections and notices in the Taxes Acts, often with individual sets of rules and time limits. Many of these claims, elections and notices exist to provide taxpayers with some degree of choice (in addition to the right to make a claim) in determining a particular computational issue. For example, the choice to claim a particular treatment, or the choice to claim a particular portion of a relief in a particular period. In all cases a formal 'claim' 'election' or 'notice' is required because the Revenue needs to know what reliefs are to be given, and which choice the taxpayer wishes to exercise, in order to include that correct figures in the relevant tax calculations and assessments.
- 6.2 The existing procedures for **claims** require the active participation of the Revenue to establish a claim as valid, and to agree the computational value of the claim, whether in terms of tax or otherwise. **Elections** require unilateral action by the taxpayer, normally, but not always, by a formal **notice** in writing. And an election normally only determines the particular basis on which a tax liability is computed.
- 6.3 There is a general time limit for claims that applies whenever the rules for a particular claim do not specify a time limit. Where this general time limit applies a claim must be made within 6 years of the end of the period (for example the tax year) to which it relates (S.43(1) TMA 1970). This limit may be extended where assessments are made after the general time limit has elapsed (further assessments, S.43A TMA 1970; discovery assessments, S.36(3) TMA 1970).
- 6.4 There is no general time limit for elections. Instead the rules applying to each election specify the time (or period) by which the election must be made.

### Claims, elections and notices under Self Assessment

- 6.5 Under Self Assessment there will be a comprehensive set of procedures for all claims, elections and notices made, or required to be made, by individuals partnerships, or companies under the Taxes Acts.
- 6.6 Wherever possible a claim, election or notice is to be included in a self-assessment return (or an amendment to a return). In this way the taxpayer will automatically notify his chosen options by means of the entries in the return or the associated self-assessment. Where the claim results in a repayment of tax the repayment will usually be made subject only to the security checks which are an integral part of the repayment process. The return as a whole, including the claim, will remain subject to the 'check later' regime.
- 6.7 Where it is not practicable to include the claim, election or notice in a return the claim will, none the less, be subject to the same type of 'process now-check later' regime that will apply to returns.
- 6.8 This means that whichever way a claim, election or notice is made it will usually be given effect to automatically, with, where appropriate (and subject only to security checks), a repayment of tax. But equally the Revenue will then have an automatic right to verify the validity and accuracy of the claim, election or notice within a specified time limit. In certain areas of particular risk, for example claims by non-residents, the Revenue may exercise its right to verify the claim before any payment is made.

## Time at which the new rules will apply

### *Section 103(7) FA 1995*

6.9 The new procedures for claims, elections and notices first apply

- **from 6 April 1996** for individuals and partnerships;
- in the case of a company to any claims, elections and notices relevant to **accounting periods ending on or after 'the appointed day'** (see paras 8.8 and 8.9).

## Terminology used in this chapter

### *Section 42(10)*

6.10 Unless otherwise stated the procedures for 'claims' in **Section 42** and **Schedule 1A** also apply to any 'elections and notices' required under the Taxes acts. In this chapter the term 'claim' is used as shorthand for 'claims, elections and notices'.

## Claims, elections and notices included in returns

### *General procedures for making claims*

## Wherever possible claims should be included in a return

### *Sections 42(1), (2), & (10)*

6.11 The general rule is that wherever possible, any claim provided for in the Taxes Acts must be included in a return, or an amendment to a return.

6.12 Where a claim is included in a return it will subject to the same 'process now - check later' procedures as any other entry in the return. For example, the Revenue will have the right to repair obvious mistakes or errors in a claim (e.g. **Section 9(4)**). It will also have the right to formally review the validity and accuracy of a claim (e.g. by means of **Section 9A**) including the right to request any information or documents relating to the claim (e.g. by means of **Section 19A**).

## Claims must be quantified at the time they are made

### *Sections 42(1A)*

6.13 A claim for a relief, allowance or repayment of tax must be quantified at the time the claim is made. It will not be possible to make a 'provisional' claim in an estimated amount. (This rule applies to claims, but not elections or notices.)

6.14 This rule must be considered in conjunction with the guidance given on the use of provisional figures in returns (*paras 2.53 to 2.54*). **Section 42(1A)** is intended to deny claims anticipating relief that may or may not arise at some future point in time. For example, if a business is doing badly the owner may think that it is 'making a loss'. But until the relevant accounting period has ended there is no certainty that there is in fact a loss for tax purposes.

- 6.15 However, where, for example, a loss has been established, but the exact amount of that loss cannot be finalised before a return is filed, the taxpayer's 'best estimate' will be acceptable as quantification of the claim. As with any other estimate the claimant will be expected to provide the final figure as soon as it is available.
- 6.16 A claim made in respect of an allowance or relief that, by its nature, is fixed in amount (for example, a personal allowance) will be treated as a claim 'quantified at the time made' even if the person making the claim does not know the actual amount due.

### Exceptions to the general rules

- 6.17 Certain claims are specifically excluded from the requirement to include a claim in a return. They are claims that will be given effect by
- a PAYE coding adjustment (*paras 6.19 to 6.21*; such claims are also excluded from the requirement to quantify the claim); or
  - a carry back of relief to an earlier year (*paras 6.22 to 6.28*).
- 6.18 In addition the general time limit of 5 years 10 months for claims (**Section 43(1)** - see *para 6.65*) means that in many cases a claim for a particular year will be made *after the return for that year has become final*. In any such case the **Schedule 1A** procedures must be used (*paras 6.32 to 6.59*).

### Claims given effect by a PAYE coding adjustment

#### **Section 42(3)**

- 6.19 Most employees do not have to complete tax returns. This is because wherever possible the PAYE system is used to collect the correct amount of tax. If, at the end of the year, the taxpayer has paid too much tax the tax overpaid is repaid automatically without the need for a formal claim.
- 6.20 The requirement to include a claim in a return does not apply where that claim will be given effect by an adjustment to a PAYE coding. This is because a claim given effect in this way is allowed before the return for the year is issued.
- 6.21 An employee who wishes to have his code number adjusted during the course of a tax year will be able to use the **Schedule 1A** procedures (*paras 6.32 to 6.59*) to make the claim outside a return.

### Claims given effect by a carry back of a relief to an earlier year

#### **Sections 42(3A) & (3B)**

- 6.22 The requirement to include a claim in a return does not apply where that claim will be given effect by a 'carry back' of a relief to an earlier year. For example, a carry back of relief for trading losses or for payments of qualifying retirement annuity premiums.

6.23 This is because it is necessary to recognise that such a claim

- is established in one year ('the later year'), but
- is given effect by reference to the tax liability of a different year ('the earlier year').

In any such case the claimant has the flexibility to choose to wait to include the claim in the return for the later year, or to make an immediate claim through the **Schedule 1A** procedure. And a claim made in 'a later year' does not interfere with the agreement of the liability of an earlier year, or extend the time limit for enquiries by 're-opening' an earlier year. This maintains the principle that a return filed on the normal filing date for a year will become final within 12 months of that filing date (unless the Revenue open an enquiry into the return), one of the key elements of Self Assessment.

#### **All such claims to be quantified by reference to the tax overpaid in 'the earlier year'**

##### **Sections 42(3A)(c) & (3B)**

6.24 The claim **is to be quantified in terms of the tax overpaid in 'the earlier year'**. The tax 'overpaid' is the tax that would not have been due in the self-assessment made for 'the earlier year' if the claim had been included in the return for that 'earlier year'.

6.25 Where no return was actually issued for 'the earlier year' the claim is to be quantified in terms of the tax that would not have been due *if* a self-assessment had been made for that 'earlier year' without including the claim now made.

#### **But any such claim is to be given effect in 'the later year'**

##### **Section 42(3A)(d)**

6.26 However, the claim **will be given effect as a claim of 'the later year'**. This means that although the claim is quantified by reference to 'the earlier year' it is none the less a claim **for the year in which the event occurs which gives rise to the relief (for example, the year in which the loss accrues or pension payments are made)**. The claim will be given effect by adjustment to the balancing payment (or repayment) due for 'the later year' or by set off in that year. It will not be necessary to revise or re-open the self-assessment for 'the earlier year'.

6.27 These rules do not alter the amount of relief given in respect of any claim or the tax effect.

6.28 But whatever the means of giving effect to the claim any repayment supplement (or interest charge) arising will be calculated by reference to the **normal filing date of 'the later year'** (the date on which any balancing payment for the year will be due).

## Claims, elections and notices not included in returns

### *Introduction*

#### **A 'process now - check later' scheme will apply to any claim not included in a return**

##### ***Section 42(11) and Schedule 1A***

- 6.29 Where a claim is included in a return the Revenue can use the normal enquiry procedures for returns to check the validity and accuracy of the claim. These procedures will allow the Revenue to check the claim on its own, or to include any such enquiry in a general review of the whole return.
- 6.30 But the enquiry procedures described in Chapter 4 cannot be applied to any claim **not included in a return, or not forming the basis of an amendment to a return**. Therefore there are a parallel set of 'process now - check later' procedures to deal with the making, and checking, of any such claims.
- 6.31 **Schedule 1A** also provides a framework for establishing the finality of any claim made outside a return.

### *Procedures for making claims other than in a return*

#### **There will be formal procedures for all claims**

##### ***paras 2(1) & (3), Schedule 1A***

- 6.32 Under Self Assessment a claim made outside a return will only be valid if
- it is made to an officer of the Board (or, where appropriate the Board), and
  - where a particular form has been prescribed by the Board, in that form.

#### **Information required in a claim**

##### ***para 2(4) Schedule 1A***

- 6.33 All claims must include a declaration that the particulars given are correctly stated '*to the best of the information and belief of the person making the claim*'.

##### ***para 2(2) Schedule 1A***

- 6.34 And in the case of a claim requiring repayment of tax a claim may only be made if the claimant has documentary proof of the tax paid.

*paras 2(5) & (6) Schedule 1A*

6.35 Where the form of the claim has been prescribed the rules provide general guidelines as to what information made be required with the claim:

- a statement of the amount of tax involved;
- any information as may reasonably be required to verify the validity and accuracy of the claim;
- in the case of chargeable gains, details of assets.

6.36 In addition the taxpayer may be asked to provide the following with the claim:

- any accounts, statements or documents as may reasonably be required to verify the validity and accuracy of the claim;
- in a claim, election or notice by non-residents, or a claim connected with residence status, any statement or declaration is to be made by affidavit.

*Amendments of claims*

**The Revenue will be able to repair the claim during initial processing**

*para 3(1)(a), Schedule 1A*

6.37 An officer of the Board may 'repair' obvious mistakes or errors in a claim. Any such amendment must be made within the 9 months following the date on which the claim is made. The taxpayer may, in turn, reject or amend the 'repair' if he or she considers it to be wrong.

**And the claimant may make amendments providing the claim is not under enquiry**

*para 3(1)(b) & (2), Schedule 1A*

6.38 Similarly, a claimant may amend a claim at any time during the 12 month period following the date on which it is made.

6.39 But a claimant may not amend a claim during any period in which the claim is under enquiry. Instead the claimant will have the right to make an appropriate amendment once the enquiry is complete.

## *Giving effect to claims*

**Unless a claim is under enquiry it must be given effect as soon as is practicable**

### *para 4, Schedule 1A*

6.40 Once a claim (or a subsequent amendment) has been made the officer of the Board (or the Board) must normally give effect to that claim '*as soon as practicable*'. This may mean

- that tax is discharged or repaid;
- that coding adjustments are made to reduce or repay tax through PAYE;
- that, in the case of a partnership, a discharge or repayment of tax is made for each partner.

6.41 Where a claim is subject to enquiry the action required to give effect to the claim need not be taken until that enquiry is complete. However, the officer of the Board making the enquiry has the discretion to give effect to the claim, in whole or in part, on a provisional basis.

## *Record keeping requirement*

**Claimants will be required to keep the records on which a claim is based**

### *paras 2A(1), (2) & (3), Schedule 1A*

6.42 A claimant will be required to keep and preserve the records needed to make a correct and complete claim. Any such records must be kept until the later of

- the date on which a formal enquiry into the claim is treated as complete;
- the date on which it becomes impossible for any such enquiry to be opened.

**Penalty for failure to keep or retain records**

### *para 2A(4) Schedule 1A*

6.43 A penalty of up to £3,000 may be charged for each failure to keep or preserve adequate records in support of a claim.

## *Enquiries into validity of claims*

### **The Revenue will be entitled to enquire into any claim**

#### *para 5, Schedule 1A*

- 6.44 As with returns the Revenue will have a formal right to make enquiries into the accuracy of any claim (or a subsequent amendment).
- 6.45 The Revenue must give the claimant written notice of the intention to enquire into the claim. Only one such notice may be given in respect of any particular claim. This is the case whether the notice of enquiry is given under *para 5 Schedule 1A*, or, if the claim is subsequently included in a return, a notice of enquiry is given in respect of the return.
- 6.46 A written notice of enquiry must be issued by the later of
- the quarter date following the first anniversary of the date on which the claim (or subsequent amendment) was made;
  - where the claim (or subsequent amendment) relates to a year of assessment the first anniversary of the normal filing date (31 January) for a return for that year;
  - where the claim (or subsequent amendment) relates to a period other than a year of assessment the first anniversary of the end of that period.

### **Where no notice of enquiry is issued the claim is final**

- 6.47 It is the dates in *para 5, Schedule 1A* that establish the point at which a claim becomes final (unless it is under enquiry, or there is a discovery relating to that claim).

### **Requests for documents, accounts or particulars**

#### *para 6, Schedule 1A*

- 6.48 The officer of the Board making an enquiry may issue a formal notice requiring the production of documents, accounts or other written particulars. This notice may be issued at the same time as the notice of enquiry, or at some later date. The claimant must be given at least 30 days to comply with the request.

### **Procedures relating to requests for documents the same as for returns**

#### *para 6(3), Schedule 1A and Section 19A(3) to (11)*

- 6.49 All the procedures relating to requests for documents, accounts or particulars relating to a return apply to requests relating to a claim (*see paras 4.42 to 4.62*).

## *Settlement of an enquiry*

### **Amendment of claims following an enquiry**

#### *para 7(4), Schedule 1A*

6.50 A formal enquiry into a claim (or a subsequent amendment) will be treated as complete when the officer of the Board issues the taxpayer with a notice to that effect. Any such notice must state the officer's conclusions regarding the claim.

### **Application for direction that an enquiry is complete**

#### *para 7(5), Schedule 1A and Sections 28A(6) & (7)*

6.51 It may be that during the course of an enquiry a claimant considers that the officer of the Board has no reasonable grounds for continuing the enquiry. In any such case the claimant may apply to the Commissioners seeking a notice stating that the enquiry is complete.

### **Amendments by claimant following completion of enquiry**

#### *para 7(2), Schedule 1A*

6.52 In the 30 days following the date on which an enquiry is treated as complete the claimant may amend the claim in respect of

- amendments required as a result of the enquiry, and
- any additional amendments (providing they are formally notified to the officer as such). For example, any amendments that the taxpayer would have made earlier under *para 3, Schedule 1A*, but which could not be made because an enquiry had been opened.

### **Further amendment by the officer of the Board**

#### *para 7(3), Schedule 1A*

6.53 Where the officer of the Board believes that the claim amended under *para 7(2) Schedule 1A* is incorrect he or she may correct that claim. Any such amendment must be made by notice within the 30 days following the passing of the 30 day time limit for amendments by the claimant.

### **Appeals against amendments by the officer of the Board**

#### *para 9, Schedule 1A*

6.54 The claimant has a right of appeal against an amendment by an officer of the Board under *para 7(3), Schedule 1A*.

6.55 Any appeal must normally be made in writing within 30 days of the date on which the notice was issued. But in the case of

- claims under S.278 ICTA 1988 (personal reliefs of non-residents);
- questions of residence or domicile;
- application of S.615(3) ICTA 1988 (pension funds for service abroad)

the time limit is **3 months**.

### **Giving effect to amendments made after completion of an enquiry**

#### ***para 8, Schedule 1A***

6.56 Once an enquiry has been completed, and amendments have been notified under either ***para 7(2)*** or ***para 7(3)***, ***Schedule 1A*** an officer of the Board is required to give effect to the claim as amended.

6.57 This may mean

- that an assessment is made on the claimant;
- that tax is discharged or repaid (subject to proof of payment);
- that, in the case of a partnership, an assessment, or as the case may be a discharge or repayment of tax is made for each partner.

6.58 All such adjustments must be made within 30 days of the notification of the relevant amendment.

#### ***para 9(4), Schedule 1A***

6.59 The same procedures apply following a decision by the Commissioners on an appeal against an amendment by an officer of the Board.

### *Miscellaneous provisions on claims*

#### **Supplementary claims**

##### ***Section 42(9)***

6.60 A taxpayer may make a supplementary claim where an error or mistake has been discovered in the original claim, providing the time limit for making the original claim has not expired. This rule applies whether the original claim was made using the ***Section 42*** or ***Schedule 1A*** procedures.

## Claims, elections and notices that must be made on behalf of a partnership

### *Section 42(6) & (7)*

6.61 There are a number of claims, elections and notices in the Taxes Acts that must be made on behalf of a partnership as if it were an individual. These may be made by either

- **Section 42** procedures by inclusion in a partnership return, or
- **Schedule 1A** procedures. In any such case the partners may nominate one of their number to make the claim.

6.62 A list of the claims, elections and notices that must be made at partnership level is included at **Section 42(7)**.

### Claim by a company to payment of a tax credit

#### *Sections 42(4) and (4A)*

6.63 A claim by a company for payment of a tax credit must normally be made in a corporation tax return. However companies that are exempt from tax, such as charities and some friendly societies, do not normally have to complete returns at all. Such companies will still be able to claim tax repayments outside of a return as now.

### Claims by trustees, guardians, tutors and curators

#### *Section 42(8)*

6.64 Trustees, guardians, tutors and curators may make claims, on behalf of incapacitated persons. Similarly, anyone assessed in a representative capacity may make a claim for the repayment or discharge of tax.

### *Time limits for claims*

#### *Section 43(1)*

6.65 The general time limit for making claims, where not otherwise specified, will be

- for individuals and partnerships **5 years from the annual filing date** (31 January) for the tax year to which the claim relates;
- for companies **6 years from the end of the accounting period** to which the claim relates.

### *Consequential amendments*

#### *Schedule 19 FA 1994*

6.66 FA 1994 and FA 1995 contain a few consequential amendments to the existing legislation for claims, elections and notices. These amendments are required to amend references to procedures, and to amend time limits. Further legislation will be required in FA 1996.

<b>TMA</b>	<b>Subject</b>	<b>Nature of amendment</b>
<i>Section 33(1)</i> (as amended by para 36(1) & (2), Schedule 19 FA 1994)	Error or Mistake relief	Time limits for claims
<i>Section 43A(1)</i> (as amended by para 15, Schedule 19 FA 1994)	Claims and further assessments	Application restricted to discovery assessments ( <i>Section 29</i> )
<i>paras 1 &amp; 2, Schedule 2</i> (as amended by para 36(1) & (2), Schedule 19 FA 1994)	Jurisdiction on claims	Change to procedures
<i>para 3, Schedule 2</i> (as substituted by para 36(3), Schedule 19 FA 1994)	Jurisdiction on claims	Change to procedures
<b>ICTA</b>		
<i>Section 96</i> (as amended by para 37, Schedule 19 FA 1994)	Farmers averaging	Time limits for claims
<i>Sections 534 &amp; 537B</i> (as amended by paras 39 & 40, Schedule 19 FA 1994)	Relief for copyright payments and designs	Time limits for claims
<i>Sections 536 &amp; 537B</i> (as amended by S.115(10) FA 1995)	Taxation of royalties where owner abroad	Change to procedures
<i>Schedule 5</i> (as amended by para 36(1) & (2), Schedule 19 FA 1994)	Herd basis	Time limits for claims

### *Conversion table*

<b>TMA 1970</b>		<b>FA 94 and FA 95</b>
<i>Section 42</i>	as substituted by	para 13, Schedule 19 FA 1994 and Section 107 FA 1995
<i>Section 43(1)</i> <i>Schedule 1A</i>	as amended by as substituted by	para 14, Schedule 19 FA 1994 para 35, Schedule 19 FA 1994 and Schedule 20 FA 1995

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# Introduction

## Scope of this chapter

- 7.1 The move to self-assessment requires that the liabilities, rights and responsibilities of taxpayers and their representatives be defined as clearly as possible.
- 7.2 However, many of the existing statutory rules in *Part VIII TMA 1970* for taxing non-residents are unclear, or redundant, and have to be applied in conjunction with Extra Statutory Concessions in order to obtain a workable and equitable system. This is not appropriate in a system of self-assessment.
- 7.3 The *Finance Act 1995* introduces new rules to replace the existing mixture of law, concession and practice with clear legislation. These have, broadly, the same overall effect as before. Some changes to the former concessions and practices are necessary, however, to put them on a clear and consistent legislative basis.
- 7.4 The new legislation reflects the principles of international taxation as set out in the OECD Model Tax Convention and UK Double Taxation Agreements (except that there is no requirement for a trade, profession or vocation to be carried out through a permanent establishment before it can be taxed as that would allow trades carried on in the UK from a tax haven to escape tax). The principles are:
- **the territoriality principle:** the source country has
    - full taxing rights over a non-resident's income from a trade, profession or vocation, or from property or an employment in that country;
    - partial taxing rights over a non-resident's interest, dividends and royalties (generally exercised by deduction of tax at source).
  - **the arm's length principle:** the taxable profits from carrying on a trade in the source country are measured on the arm's length principle, that is the profits that would arise if the part of the business in the country and the part outside were carried on by independent persons acting at arm's length.
- 7.5 The new legislation provides rules in the following areas:
- agents and tenants to account for tax on UK property income of non-residents;
  - the liabilities and obligations of UK representatives of non-residents;
  - persons not to be treated as UK representatives of non-residents;
  - the limits of income and corporation tax chargeable on non-residents;

This chapter contains a summary of these new rules. Taxpayers should bear in mind, in reading the summary, that the tax liabilities of non-residents can be complex. They are advised to seek professional help if they are in any doubt as to how the new rules will apply to them.

7.6 The new legislation also provides rules in the following two areas:

- the tax treatment of an individual in business following a change in residence status;
- special rules for non-resident partners.

These rules are considered in more detail in *Chapter 11* of SAT1.

## *Taxation of UK property income of non-residents*

### **Purpose of the rules**

7.7 UK tax law and Double Taxation Agreements give the UK full taxing rights over the income of non-residents from property in the UK. These are currently exercised through a combination of deduction at source and assessment on the tenant, the agent and the taxpayer. There are two separate and, in some cases, overlapping schemes for collecting the tax: S.43 ICTA 1988 which requires tenants to deduct tax at source from gross rents payable direct to overseas landlords; S.78 TMA 1970 which allows branches and agents to be taxed on behalf of a non-resident.

7.8 The new rules introduced by *FA 1995* are based on a single scheme for tenants and agents. Property agents (or, where there is no agent, the tenants), will account for tax at the basic rate on property income net of expenses paid. The non-resident will be able to set off any tax suffered by the agent against the corresponding tax due in his or her self-assessment. But the new rules will allow rent to be paid **gross** if the non-resident wishes and the Inland Revenue agrees.

### **Circumstances in which the new rules apply**

#### ***Section 42A(1) and (2) ICTA 1988***

7.9 The new rules will apply to property agents who:

- act on behalf of persons whose usual place of abode is outside the UK ('non-residents'); and
- receive property income, or have control over property income, of the non-resident.

7.10 Where there is no such property agent acting, the rules apply to the tenants instead.

### **Right of retention for agents and tenants**

#### ***Section 42A(3) ICTA 1988***

7.11 An agent (or tenant) within the scheme will be entitled to retain sufficient sums out of the property income to meet any tax liabilities arising. The agent will also be entitled to be indemnified by the non-resident for sums due under the new rules.

## **The arrangements will be in Regulations made by the Board of Inland Revenue**

### ***Section 42A(1) and (4) ICTA 1988***

7.12 Details of the scheme will be provided in regulations made by the Board of Inland Revenue. These Regulations will be made well in advance of 6 April 1996, the date the scheme comes into operation. They will

- prescribe the person who must operate the scheme;
- provide that the prescribed person must
  - compute and account for tax (on a quarterly basis) at the basic rate on property income less expenses;
  - complete an annual information return showing property income, expenses and the tax liability arising in respect of each non-resident for which they act;
  - provide each non-resident for which they act with a certificate for the tax year, showing the prescribed person's tax liability. The non-resident will set-off this tax in his or her self-assessment for the year.

Agents will compute tax on property income **received** in the quarter less expenses paid in the quarter. Tenants will compute tax on property income **paid** in the quarter (excluding property income withheld by the tenant to meet allowable expenses paid on behalf of the non-resident).

## **The Regulations will allow for rent to be paid gross In certain circumstances**

### ***Section 42A(4) ICTA 1988***

7.13 Non-residents will be able to apply to the Inland Revenue to receive property income gross on the basis that

- they do not expect to be liable to UK tax, or
- they do not have a poor tax history and will comply fully with Self Assessment.

## **Interest and penalties**

### ***Section 42A(4), (5) ICTA 1988 and Section 98***

7.14 Agents (and tenants) will be liable to interest if tax is paid late, and to penalties (under **Section 98**) for any failure to comply with the obligations set out in the regulations.

## **Time at which the new rules will apply**

### ***Section 40(3) FA 1995***

7.15 The new rules will apply to **any payments made on or after 6 April 1996**.

## *UK representatives of non-residents chargeable under Case I & II Sch.D*

### **Introduction**

- 7.16 Under the existing rules - S.78(1), 83, 84 and 85 TMA 1970 - almost any person acting for a non-resident in any capacity, however small, could be held responsible for the non-resident's tax affairs. These rules are very wide and have become outdated. They have been cut down in practice through administrative discretion but that is not appropriate for Self Assessment.
- 7.17 **FA 1995** introduces new rules for taxing the UK liabilities of non-residents on their UK representatives. These rules define clearly:
- who is liable to UK tax,
  - who is responsible for complying with the tax obligations,
  - the nature and extent of those obligations.

### **The UK representative rules will apply to all non-residents**

#### ***Section 126(1) FA 1995***

- 7.18 The new rules define the obligations and liabilities of the **UK representatives** of non-residents and will apply to both non-resident individuals and companies.

### **Definition of UK representative**

#### ***Section 126(2) and (8) FA 1995***

- 7.19 Under the new rules the 'UK representative' of a non-resident is defined as the branch or agency through which the non-resident carries on any trade, profession or vocation.
- 7.20 It follows that if the non-resident is not trading in the UK through a branch or agency there can be no 'UK representative' for tax purposes. (This is narrower than the old rule which *could* apply where there was no trade, profession or vocation.) Instead the non-resident will be responsible for complying with any UK tax obligations.
- 7.21 "Branch or agency" means "any factorship, agency, receivership, branch or management" (S.118 TMA 1970).

7.22 Where a branch or agency is a UK representative it will be responsible for complying with the tax obligations arising from its activities. That is:

- the profits of the trade, profession or vocation of the non-resident carried on through the branch or agency;
- income from property or rights which are used by, or held by or for it;
- capital gains chargeable on non-residents under S.10 Taxation of Chargeable Gains Act 1992;
- (where the non-resident is an overseas life insurance company) amounts chargeable under para. 3, Schedule 19AC ICTA 1988.

(This differs from the old rules for charging branches and agencies of non-resident **individuals** where there was no trading requirement and no specific limitation on the profits chargeable. It also brings the obligations of UK representatives for non-resident individuals into line with those for non-resident companies.)

### **General rule for the obligations and liabilities of UK representatives**

#### ***paras 1, 2 and 3 Schedule 23 FA 1995***

7.23 The general rule is that UK representatives will be **jointly responsible** with the non-resident for all the tax obligations and liabilities in relation to the trade, profession or vocation carried on through the branch or agency.

7.24 This joint responsibility extends to all matters relating to the assessment of tax, and to the collection and recovery of tax. For example, it extends to all the mechanisms of Self Assessment, including notification of chargeability, the obligation to make a return and self-assessment, liability to make interim and final payments of tax, and liability to surcharges, interest and penalties in connection with those obligations and liabilities.

7.25 Either party will be able to discharge the obligations and liabilities arising. But equally any acts or omissions of the UK representative will be treated as acts or omissions of the non-resident (but see also *paras 7.31 to 7.33* in relation to tax offences).

7.26 Where the trigger for an obligation or liability is the receipt of formal notification, then the obligation or liability will only fall on the UK representative once they have received the relevant notification (or a copy).

### **Obligations and liabilities are limited where the UK representative is independent of the non-resident**

#### ***paras 4 and 7 Schedule 23 FA 1995***

7.27 Where the UK representative is an independent agent of the non-resident, its obligations to provide information are limited to ones within its competence to act for the non-resident.

7.28 "Independent agent" is defined at ***para 7 Schedule 23 FA 1995***. The definition is based on that used in the OECD Model Tax Convention and UK double taxation agreements. Broadly, to be an "independent agent", the agent must be both legally and economically independent of the non-resident.

- 7.29 The rules recognise that, where the UK representative is an independent agent, the agent may not be able to provide complete information about the affairs of the non-resident. The agent is therefore required to, provide any information requested - for example a return - to the best of its knowledge and belief after taking all reasonable steps to obtain the information. The non-resident remains responsible for completing or correcting the information where necessary.
- 7.30 However, the non-resident can correct any error or omission made by the UK representative provided the non-resident did not know about it or participate in it.

## **Offences**

### ***para 5, Schedule 23 5 FA 1995***

- 7.31 The criminal and civil liabilities of a UK representative in respect of the non- resident's tax affairs are limited in certain circumstances.
- 7.32 UK representatives cannot be guilty of a **criminal** offence under these rules as a result of something done by the non-resident unless
- they committed the offence *or*
  - consented to its commission *or*
  - connived in its commission.

The same applies for the non-resident in relation to the acts of the UK representative.

- 7.33 UK representatives who are independent agents are not liable to **civil** penalties and surcharges unless
- they committed an act or omission or consented to, or connived in, its commission *or*
  - they will be able to recover the penalty out of monies of the non-resident.

## **An independent agent can retain and recover monies due**

### ***para 6, Schedule 23 FA 1995***

- 7.34 UK representatives who are independent agents of non-residents are entitled to retain out of the non-resident's monies amounts sufficient to meet UK tax liabilities.

## **UK representative will retain any obligations and liabilities for the period of agency after the period has ended**

### ***Section 126(3) FA 1995***

- 7.35 The obligations and liabilities of a UK representative for a period during which it was the branch or agency will continue if the branch or agency ends.

## **UK representative will be treated as a separate person**

### *Section 126(4) FA 1995*

7.36 The UK representative and the non-resident will be treated as separate persons. This allows, for example, service of notices and collection to take place at the branch or agency.

## **A partnership can be the UK representative of a non-resident**

### *Section 126(5) FA 1995*

7.37 A partnership can be the UK representative of a non-resident. This will occur, for example, where a non-resident trades in the UK through the agency of a UK partnership (of which he is not a member). In such circumstances the UK partners will be jointly liable, as UK representative, for the tax payable by the non-resident.

## **Partnership, which includes non-resident partners, trading in the UK through branch or agency: branch or agency will be treated as the UK representative of non-resident partners**

### *Section 126(6) FA 1995*

7.38 Where a business that is carried on by a partnership which includes non-resident partners is carried on in the UK through a branch or agency, the branch or agency will be treated as the UK representative of each non-resident partner.

## **Partnership trading in the UK which includes resident and non-resident members will be treated as UK representative of non-resident partners**

### *Section 126(7) FA 1995*

7.39 Where a business is carried on in the UK by a partnership which includes both resident and non-resident partners, the partnership is treated as the UK representative of each non-resident partner. The partners are thus jointly liable for the tax payable by the non-resident partners on their shares of the partnership profit.

## **Time at which the new rules apply**

### *Section 126(9) FA 1995*

7.40 The new UK representative rules replace the present rules in Part VIII TMA and apply:

- from **1996/97** onwards for income and capital gains tax, and
- for corporation tax to accounting periods beginning **after 31 March 1996**.

## *Agents who are not treated as UK representatives*

### **Introduction**

- 7.41 Certain categories of agents are specifically exempted from the rules in **Section 126 FA 1995** which impose obligations and liabilities on the UK representatives of non-residents.
- 7.42 The exemptions are based on the existing rules but with certain modifications. Principal amongst these is the introduction of a more closely targeted anti-avoidance provision in relation to the exemption of investment managers. This replaces a more wide ranging rule which automatically excluded all investment managers whose non-resident client was their sole client or a connected person. That rule went wider than was generally needed to prevent abuse.

### **Exempt agents: casual agents, Lloyd's' members' agents, brokers and investment managers**

#### ***Section 127(1) and (13) FA 1995***

- 7.43 The following (who are generally treated as exempt agents at present) will not be treated as UK representatives of non-residents and therefore will not be subject to the obligations and liabilities imposed by **Section 126 FA 1995**:
- casual agents, that is, agents who are not carrying on a **regular** agency for the non resident,
  - members' agents and managing agents (as defined at **Section 127(13)**) of syndicates at Lloyd's (underwriting profits will continue to be taxable in full through Self Assessment by non-resident members in the same way as for resident members).
- 7.44 The following will not be treated as UK representatives of non-residents and therefore will not be subject to the obligations and liabilities imposed by **Section 126 FA 1995** **provided certain conditions are met**:
- brokers;
  - investment managers.

These rules continue the existing rules but with more narrowly focused anti-avoidance provisions for investment managers.

## Brokers

### *Section 127(1)(b) and (2) FA 1995*

7.45 There are four conditions which must all be met before the specific exemption for brokers can apply. These are:

- the broker must be carrying on the normal business of a broker in a market where brokers normally act;
- the transaction must be carried out by the broker in the ordinary course of the broker's business;
- the broker's fee must be at least the customary fee for that class of business;
- the non-resident must not, during the same chargeable period, carry out any trading transactions through the broker other than those which are excluded by this rule.

The purpose of these conditions is to exempt only those brokers who are acting in the ordinary course of their business on arm's length terms.

## Investment managers

### *Section 127(1)(c) FA 1995*

7.46 The four conditions applying to brokers are mirrored in the conditions which must be met before the exemption for investment managers can apply. These are:

- the investment manager must be carrying on the business of providing investment management services;
- the transaction must be carried out by the investment manager in the ordinary course of the investment management business;
- the investment manager's fee must be at least the customary fee for that class of business;
- the non-resident must not, during the same chargeable period, carry out any trading transactions through the investment manager other than those which are excluded by this rule.

7.47 In addition, there are three further conditions which must also be met:

- the transactions must be investment transactions: (*paras 7.49-7.51*);
- the investment manager must act on behalf of the non-resident in an independent capacity: (*paras 7.52-7.55*);
- the investment manager must not be entitled to more than 20% of the profit from the transactions on behalf of the non-resident: (*paras 7.56-7.59*).

7.48 The purpose of these conditions is to exempt only those investment managers who are acting in the ordinary course of their business on arm's length terms and are independent of the non-resident.

## Investment managers: the investment transaction condition

### *Section 127(3), (9) and (10) FA 1995*

7.49 The investment manager exemption is intended to cover the discretionary management of financial investments. It therefore applies only where the investment manager carries out **investment** transactions on behalf of the non-resident.

7.50 "Investment transaction" is defined at *Section 127(9) and (10) FA 1995* and includes transactions in

- shares
- stock
- securities
- futures contracts (excluding those relating to land)
- options contracts (excluding those relating to land)
- foreign currency
- money placed at interest.

7.51 Most **financial instruments**, including futures and options contracts in physical commodities, are covered by this definition. Spot transactions in physical commodities (including precious metals such as gold bullion) are outside the definition.

## Investment managers: the 'independent agent' condition

### *Section 127(3)(c) and (8) FA 1995*

7.52 The exemption applies only where the investment manager is the 'independent agent' of the non-resident. This is defined in the same way as in *para 7.28* above. It requires the relationship between the investment manager and the non-resident to have the legal, financial and commercial characteristics of one between persons carrying on independent businesses that deal with each other at arm's length. Where the conditions in *Section 127 (3)(a), (b), (e) and (f) FA 1995* are also satisfied, it is considered that this definition would be satisfied:

- where the provision of services to the non-resident and persons connected with the non-resident is not a 'substantial part' (*see para 7.53*) of the investment management business;
- from the start of a new investment management business provided the above condition was satisfied within 18 months;
- where the manager intended to satisfy either of the above conditions and failed to do so for reasons outside his control, having taken any reasonable steps to fulfil the intention;
- where investment management services are provided to a collective fund, the interests in which are quoted on a recognised stock exchange or otherwise freely marketed, for instance as units in a unit trust;
- where investment management services are provided to a 'widely held' (*see para 7.54*) collective fund.

- 7.53 The provision of services to the non-resident and persons connected with the non-resident is not a 'substantial part' of the investment management business where it does not exceed 70% of that business, either by reference to fees or to some other measure where that would be more appropriate. Moreover, where investment management services are provided to a collective investment scheme constituted as a partnership, participants in the scheme would not be regarded as connected persons for this purpose solely by reason of membership of the partnership.
- 7.54 A fund is 'widely held' if either no majority interest in the fund is held by five or fewer persons and persons connected with them, or if no interest of more than 20% is held by a person and persons connected with him.
- 7.55 The above list is not exhaustive. Cases which fall outside these categories would have to be considered on their own facts. Moreover, a subsidiary is not to be considered not independent of its parent company in this regard solely because of the parent's ownership of the share capital.

### **Investment managers: the '20%' condition**

#### ***Section 127(3)(d) and (4)-(7) FA 1995***

- 7.56 This condition is satisfied where the investment manager, together with any persons connected with the investment manager (as defined at S.839 ICTA 1988), are not entitled to more than 20% of the taxable profits of the non-resident from transactions carried out through the investment manager. Where the 20% limit is exceeded the exemption will apply to the rest of the taxable profits (i.e. the part to which the investment manager and connected persons are not entitled) provided the other conditions for the exemption are satisfied.
- 7.57 The 20% rule is satisfied:
- throughout a period not exceeding five years;
  - for which the investment manager and persons connected with the investment manager;
  - intended their beneficial interest in the total taxable income for the period from transactions carried out through the investment manager not to exceed 20%;
  - provided any failure to meet the 20% limit was for reasons wholly or partly outside their control and, nevertheless, the intention was fulfilled insofar as it was reasonable to do so.
- 7.58 Performance related fees would not normally affect the operation of the 20% rule as the rule looks at the beneficial interest in the taxable profits of the non-resident from trading through the investment manager. Professional fees, including performance related fees, would normally be allowable as a deduction in arriving at those profits, and would thus be netted off before applying the 20% rule.

7.59 The provisions in **Section 127(7A) to (7D) FA 1995** ensure that where investment management services are provided to a collective investment scheme which is transparent for tax purposes, the 20% rule is applied by looking at the scheme as a whole. It is treated as satisfied by each participant in the scheme:

- where the scheme, if it were taxed as a separate entity, would not be regarded as carrying on a financial trade in the UK, whatever the level of beneficial entitlement; and
- where the scheme, if it were taxed as a separate entity, would be regarded as carrying on a trade, provided the 20% rule is satisfied in respect of the beneficial entitlement of the investment manager and connected persons to the taxable income of the scheme.

### **Time at which the new rules apply**

#### **Section 127(15) FA 1995**

7.60 The exemption rules generally apply from the same time as the UK representative rules, that is

- from **1996/97** for income and capital gains tax,
- for corporation tax to accounting periods beginning **after 31 March 1996**.

However, in relation to transactions carried out through a broker or investment manager satisfying the conditions above, the effect of the rules in **Sections 128** and **Section 129** (see 7.71 below) is to protect the representative from assessment for transactions **after 5 April 1995**.

### *Limit to charge on non residents*

#### **Introduction**

7.61 **FA 1995** introduces rules which limit the tax charge on non-residents. Broadly, they put into law what was previously achieved by extra statutory concession. The new rules are in line with the accepted principles of international taxation in the OECD Model Tax Convention and Double Taxation agreements between the UK and other countries.

#### **Income tax**

##### **Section 128 FA 1995**

7.62 In summary, the effect of these rules is that income tax chargeable on non-residents in respect of

- most types of income from investments (except property in the UK; paras 7.7 to 7.15)
- income from trading in the UK through a qualifying broker or investment manager

is limited to the tax, if any, deducted at source (provided there is no UK representative for the income).

7.63 The limitation does not apply to non-resident trusts if a current or potential beneficiary is either an individual ordinarily resident or a company resident in the UK.

## Details of the limit on income tax

### *Section 128(2) to (6) FA 1995*

7.64 The income tax charge on the non-resident is the lower of the tax that would be chargeable on the total income if personal allowances were given and the limit set by *Section 128 FA 1995*. That limit is the sum of:

- the tax which would be due on the non-resident's total income if the excluded income' (*see para 7.65*) were excluded and no personal allowances were given,

**plus**

- the tax deducted at source (including tax credits) from the 'excluded income'.

7.65 'Excluded income' is

- investment income other than income from land (any income chargeable under Schedule C, Case III of Schedule D or Schedule F);
- profits or gains from disposals of certificates of deposit (S.56 ICTA 1988);
- Social Security benefits chargeable under Schedule E (S.150, S.617(1) or S.139(1) FA 1994);
- income from transactions through investment managers or brokers which is excluded from *Section 126 FA 1995* by *Section 127 FA 1995*
- any other income designated as excluded by Treasury regulations
- provided that it is not income in relation to which the non-resident has a UK representative within *Section 126 FA 1995* (*paras 7.19 to 7.26*) or profits as a Lloyd's underwriter;

### Example: operation of *Section 128 FA 1995* limit for income tax

7.66 Assume a personal allowance of £3,000 is due and tax is at a single rate of 25%.

- A non-resident has UK income of bank interest (received gross) £10,000.

Her liability on total income is  $(£10,000 - £3,000) \times 25\% = £1,750$ .

But the bank interest is *excluded income*. Therefore *Section 115 FA 1995* restricts the liability to tax deducted at source = **nil**.

- A non-resident has UK income of bank interest (received gross) £5,000, rents £2,000 and dividends £4,000 plus tax credits £1,000.

His liability on total income is  $(£12,000 - £3,000) \times 25\% = £2,250$ .

But the bank interest and dividends are *excluded income*. Liability is limited to rents  $(£2,000 \times 25\%)$  plus the tax deducted at source (£1,000) = £1,500. The only tax to pay is **£500** on the rents.

- A non-resident has UK income of rents £4,000.

Her liability on total income is  $(£4,000 - £3,000) \times 25\% = £250$ .

The income is **not** excluded income so the *Section 128 FA 1995* limit is £4,000 at 25% = £1,000. *Section 128 FA 1995* does not reduce the charge which remains at **£250**.

### Corporation tax

#### *Section 129 FA 1995*

7.67 Corporation tax chargeable on non-residents in respect of income from trading in the UK through a qualifying broker or investment manager is limited to the tax, if any, deducted at source (provided there is no UK representative for the income).

7.68 The limitation does not apply to corporate members of Lloyd's: underwriting profits are fully chargeable to UK tax and the rules at Lloyd's restrict corporate members to underwriting and ancillary activities.

### Details of the limit on corporation tax

#### *Section 129(1)-(2) FA 1995*

7.69 The corporation tax charge for non-residents is the lower of the tax that would be chargeable on the total income of the company and the limit set by *Section 129 FA 1995*. That limit is the sum of

- the tax deducted at source (including tax credits) on any "excluded income" (see paras 7.70), plus
- the corporation tax which would be chargeable on the profits of the accounting period if the "excluded income" were not included in the profits.

7.70 'Excluded income' is income from transactions carried out through a broker or investment manager which is excluded from **Section 126 FA 1995** by **Section 127 FA 1995** other than income in relation to which the non-resident has a UK representative within **Section 126 FA 1995** (see paras 7.17 to 7.26).

#### **Time at which the new rules apply**

##### **Section 128(7) - (11) and Section 129(5) - (6) FA 1995**

7.71 The general rule is that the limitations on charge apply:

- from **1996/97** for income tax;
- for corporation tax to accounting periods beginning **after 31 March 1996**.

7.72 However, there are special rules which apply to transactions carried out before these dates through brokers and investment managers in the ordinary course of their business and for an arm's length fee:

- income tax: the limitation on charge applies for 1995/96 where income from these transactions (and certain social security benefits) would otherwise have been "excluded income" if all the UK representative rules in **Section 126** and **Section 127 FA 1995** had been in force for that year;
- corporation tax: the limitation applies to any income from these transactions which arises after 5 April 1995 which would have been 'excluded income' if all the UK representative rules in **Section 126** and **Section 127** and the corporation tax limit rule at **Section 129 FA 1995** had then been in force.

#### *Change in residence status*

##### **In future changes in residence status will trigger a deemed commencement or cessation for the purposes of assessing business profits**

##### **Section 110A ICTA 1988**

7.73 **Section 110A** provides that where an individual carrying on a business wholly or partly outside the UK becomes resident, or ceases to be resident in the UK, the business is treated as having ceased and recommenced. This is to ensure that the right amount of profits are taxed. That is profits earned world-wide while resident but only profits earned in the UK while non-resident.

7.74 Details of the operation of the new rules can be found in Chapter 11 of SAT1.

## *Non resident partners*

**In future changes in the residence status of a partner will also trigger a deemed commencement or cessation for the purposes of assessing business profits**

### ***Section 112 ICTA 1988***

7.75 ***Section 112*** provides that where a member of a partnership either becomes resident, or ceases to be resident in the UK, then for tax purposes that partner is treated as having first ceased and then immediately recommenced as a partner. The rules ensure that resident partners are taxed on their share of the world-wide partnership profits but non-resident partners only on their share of the profits earned in the UK.

7.76 The existing special rules for foreign partnerships (that is partnerships controlled and managed abroad) are restated.

7.77 Details of the operation of the new rules can be found in Chapter 11 of SAT1 paras.

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## *Introduction*

### **Self Assessment for companies subject to corporation tax will require modification of the rules introduced under 'Pay and File'**

- 8.1 A new system for dealing with the issue and delivery of corporation tax returns, and for the payment of corporation tax - 'Pay and File' - has been in operation since 1 October 1993.
- 8.2 The Pay and File system already contains many of the features that characterise Self Assessment. For instance the Pay and File return must include a computation of the corporation tax due. The return must be delivered, and the corporation tax paid, on fixed dates related to the company's accounting period. And if the return is late, or the tax paid is incorrect and therefore some tax is paid late, interest and penalties are automatically due.
- 8.3 But Pay and File does not include the process of self-assessment itself. Instead an Inspector is required to make an assessment based on the Pay and File return.
- 8.4 If the Inspector is satisfied with the Pay and File return the assessment that is issued is an assessment in the agreed figures. But if the Inspector is not satisfied with the return an estimated assessment is made. So Pay and File does not totally eliminate the estimated assessment-appeal-Commissioners listing cycle.
- 8.5 The changes required to bring Pay and File fully into line with Self Assessment are relatively straightforward. The changes required will
- give companies the same responsibility for their tax affairs as all other taxpayers, in particular it will require them to self-assess;
  - apply the same rules regarding finality, discovery assessments and Revenue enquiries to companies as will apply for all other taxpayers.

These changes mirror those described for individuals in Chapters 2 to 4.

- 8.6 No changes are required to the basic payment and filing date rules for Pay and File, or to the penalties for late payment or filing as these already provide a fixed time scale for returns and the payment of corporation tax.
- 8.7 But under Self Assessment the Revenue will not issue an assessment simply because a return is late. So the new mechanism for Revenue determinations of estimated self-assessments (*para 2.80*) will also apply to companies.

### **Time at which the new rules will apply**

#### ***Section 199 FA 1994***

- 8.8 Self Assessment will apply to companies for "*accounting periods ending on or after the appointed day*". This day, to be determined by the Treasury, will not be earlier than 1 April 1996.
- 8.9 This flexibility in the start up date for companies is simply to allow changes to be made to the Pay and File computer system without jeopardising the day to day running of the system. It is intended that the appointed day will be no later than 31 March 1998.

## **Application of the fixed return and payment time scale introduced by 'Pay and File' for Self Assessment purposes**

- 8.10 Under Pay and File the normal due date for the payment of corporation tax is 9 months after the end of the accounting period on which the return is based (S.10(1)(a) ICTA 1988).
- 8.11 Where the return was issued at the normal time the filing date for the corresponding return is 12 months after the end of the accounting period (S.11(4) TMA 1970).
- 8.12 Where the return was issued late (that is more than 9 months after the end of the accounting period) the filing date is the date 3 months after the date of issue of the return (S.11(4) TMA 1970).
- 8.13 Where, in Chapters 2 to 4, the Self Assessment rules operate by reference to the due dates for payment, or to filing dates, the Pay and File filing dates will be those which apply for companies.
- 8.14 The "chargeable period" for a company is its accounting period. So wherever, in Chapters 2 to 4, the Self Assessment rules operate by reference to a tax year for individuals, they operate by reference to accounting periods for companies.

### ***Sections 34, 36 & 43***

- 8.15 For a company the normal time limit for discovery assessments not involving fraudulent or negligent conduct, claims, etc. is 6 years from the end of the relevant accounting period. So where, in Chapters 2 to 4, the Self Assessment rules define a time limit as 5 years from the normal filing date for a tax year (i.e. approximately 5 years 10 months after the end of that tax year), the corresponding time limit for a company is 6 years from the end of the relevant accounting period.
- 8.16 Similarly the time limit for a discovery assessment involving fraudulent or negligent conduct is 21 years from the end of the relevant accounting period.

### ***Summary of specific Self Assessment legislation for companies***

#### **Partnership income**

##### ***Section 11(2A) & (2B)***

- 8.17 A company will be required to deliver a return of total income like any other taxpayer. So the corporation tax return will have to include a company's share of any partnership profits. As with individuals, this share must equal the share allocated to the company in the partnership statement.

#### **Corporation tax returns will include a self-assessment**

##### ***Section 11AA***

- 8.18 A corporation tax return will have to include a self-assessment.
- 8.19 Virtually the same rules apply to companies as to individuals. But there is no rule requiring the Revenue to calculate the tax due if the return is delivered early.
- 8.20 The rules for repairs to returns, and taxpayer amendments, mirror those for individuals, including time limits of 9 and 12 months (from the filing date).

## Power to enquire into corporation tax returns

### *Section 11AB*

- 8.21 The enquiry powers relating to company returns mirror those for individuals, including the 12 month and quarter day time limits for finality.

## Payment of corporation tax

### *Section 59D*

- 8.22 There are no changes to the rules for the payment of corporation tax introduced by Pay and File. But the rules have been moved from their current position (S.10 ICTA 1988) to *Section 59D* so that all the rules for the payment of tax are together in the same section of the same Act.

## Penalties and interest

- 6.23 There are no changes to the automatic penalty and interest regime for corporation tax which was introduced with Pay and File (S.87A, 94, 96 & 97A TMA 1970).

## Other legislation

- 8.24 In addition to the specific legislation outlined above the following Self Assessment sections apply for corporation tax purposes as they apply for income tax and capital gains tax purposes. In these sections the relevant returns are returns under *Section 11*.

<i>Section 12B</i>	Requirement to keep documents
<i>Section 19A</i>	Power to call for documents
<i>Section 28A</i>	Amendment of self-assessment after an enquiry
<i>Section 28C</i>	Determination of tax where no return delivered
<i>Section 29</i>	Assessment of tax where loss of tax discovered
<i>Section 30</i>	Recovery of tax overpaid
<i>Section 30A</i>	Assessing procedures
<i>Section 30B</i>	Amendment of partnership statement where loss of tax discovered
<i>Section 31</i>	Rights of appeal
<i>Section 33</i>	Error or mistake relief
<i>Section 42</i>	Procedure for making claims etc.
<i>Section 43A</i>	Further assessments: claims etc.
<i>Section 46</i>	Determination of Commissioners
<i>Section 50</i>	Procedures on appeal
<i>Section 55</i>	Postponement of tax pending appeal
<i>Section 70</i>	Payments by cheque
<i>Section 97AA</i>	Penalties for failure to deliver documents under <i>Section 19A</i>

## *Conversion table*

### TMA 1970

### FA 94 and FA 95

<i>Section 11(2A)</i>	as inserted by	Section 181(3) FA 1994
<i>Section 11AA</i>	as inserted and amended by	Section 182 FA 1994 and Section 104(5) FA 1995
<i>Section 11AB</i>	as inserted by	Section 183 FA 1994
<i>Section 59D</i>	as inserted by	Section 195 FA 1994

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## *Introduction*

- 9.1 There are a considerable number of “consequential amendments” in FA 1994 and FA 1995. These amendments modify legislation in TMA 1970, and elsewhere, to reflect the new language, procedures, rights and obligations which will apply in the Self Assessment regime detailed in previous chapters.
- 9.2 The consequential amendments in FA 1994 are changes primarily associated with
- the construction and use of the term “assessment” (*paras 9.4 to 9.8*)
  - the new time limits for claims etc. which reflect the new timetable for making returns (*paras 9.9 to 9.10*)
- 9.3 The consequential amendments in FA 1995 are primarily concerned with changes in the rules for particular groups of taxpayers. In particular
- employees (*paras 9.11 to 9.24*)
  - trustees, personal representatives and the beneficiaries of estates (*paras 9.25 to 9.50*)

## *Construction and use of the term “assessment”*

### **Use of the term “assessment” in the Taxes Acts will cover both self-assessments and Revenue assessments**

#### ***Section 197 FA 1994***

- 9.4 Under Self Assessment there will be both “self-assessments”, that is
- a self-assessment forming part of a return (e.g. under ***Section 9***)
  - an amended self-assessment following a repair (e.g. under ***Section 9(4)***) or an enquiry (e.g. under ***Section 28A***)
  - a determination under ***Section 28C*** (which is treated as if it were a self-assessment) following a failure to make a return
- and “Revenue assessments”, that is
- a discovery assessment made under ***Section 29*** to make good a loss of tax.
- 9.5 All references in the Taxes Acts to the process of assessing a person to tax, or to the process of creating a charge to tax by an assessment, will cover both self-assessments and Revenue assessments.

### **Consequential amendments to language used in TMA 1970**

- 9.6 In addition to the general rule regarding the construction of the word “assessment” the language used in TMA 1970 has been amended so that it applies equally to the self-assessment process and the Revenue assessment process. For example references to the “making” of assessments have been replaced by more neutral terms such as “securing that .... are assessed” (***Section 12A***).

9.7 Many of these changes have been dealt with in earlier chapters. Those that have not been considered in any detail are included in the table below.

9.8 The following table summarises the consequential amendments concerned with the term 'assessment' and related procedures that have not been dealt with in detail in earlier chapters:

<b>TMA</b>	<b>Subject</b>	<b>Nature of amendment</b>	<b>Location</b>
<i>Section 12A(2)</i>	Issue of returns to European Economic Interest Groupings	Reference to assessment	para 2, Schedule 19 FA 1994
<i>Section 31(1) to (3)</i>	Right of appeal	Extension to cover appeals in connection with self-assessments	para 7, Schedule 19 FA 1994
<i>Section 43A(1)</i>	Claims and further assessments	Restriction to discovery assessments ( <i>Section 29</i> )	para 14, Schedule 19 FA 1994
<i>Section 46(2)</i>	Determination of the Commissioners	Determinations final subject to discovery ( <i>Section 29</i> )	para 16, Schedule 19 FA 1994
<i>Section 50(6) &amp; (7)</i>	Procedure on appeal	Extension to cover appeals in connection with self-assessments	para 17, Schedule 19 FA 1994
<i>Section 55(1) to (11)</i>	Postponement of tax pending appeal	References to "assessment" and extension to include self-assessment	para 18, Schedule 19 FA 1994
<b>ICTA 1988</b>			
S.73 ICTA 1988	single assessments for Cases III, IV or V	(repealed)	Section 115(9) FA 1995
<i>Sections 536 &amp; 537B</i>	Taxation of royalties where owner abroad		Section 115(10) FA 1995
Sch.3 ICTA 1998	machinery provisions for assessments	(repealed)	Section 115(11) FA 1995
<b>TCGA 1992</b>			
S. 7 TCGA 1992	due date for capital gains tax assessments	(repealed)	Section 115(12) FA 1995

## *Revision of time limits*

9.9 Under the Self Assessment regime all general time limits, for example for the making of a claim, will run by reference to the normal filing date for returns. So for income tax and capital gains tax purposes the time limit runs by reference to 31 January following the tax year to which the return relates. For corporation tax purposes the time limit runs by reference to the 12 month anniversary of the accounting period to which the return relates.

9.10 The following table summarises the consequential changes concerned with time limits that have not been dealt with in detail in earlier chapters.

<b>TMA</b>	<b>Subject</b>	<b>Nature of amendment</b>	<b>Location</b>
<i>Section 30(5)</i>	Recovery of overpayment of tax	Time limits	para 4(2), Schedule 19 FA 1994
<i>Section 33(1)</i>	Error or Mistake relief	Time limits	para 8, Schedule 19 FA 1994
<i>Section 34(1)</i>	General time limit for assessments	Time limits	para 10, Schedule 19 FA 1994
<i>Section 36(1)</i>	Time limit for discovery assessments	Time limits	para 11(1), Schedule 19 FA 1994
<i>Section 40(1) &amp; (2)</i>	Time limits for assessments on personal representatives	Time limits	para 12, Schedule 19 FA 1994
<i>Section 103(2)</i>	Time limit for penalty proceedings	Time limits	para 32, Schedule 19 FA 1994
<b>ICTA 1988</b>			
<i>Section 96</i>	Farmers averaging	Time limits	para 37, Schedule 19 FA 1994
<i>Sections 534 &amp; 537B</i>	Relief for copyright payments and designs	Time limits	paras 39 and 40 Schedule 19 FA 1994
<i>Schedule 5</i>	Herd basis	Time limits	para 43, Schedule 19 FA 1994

## Self Assessment for employees: consequential amendments for PAYE purposes

*Self Assessment will only apply to those employees who get tax returns.*

### Who will get tax returns?

9.11 Around 25 million people are currently covered by the Pay As You Earn (PAYE) system. Up to 5 million of them will be sent tax returns and required to self-assess. These will be people who have relatively complicated tax affairs.

### Information required in the Returns

9.12 The information required will be that needed to calculate the taxpayer's total taxable income (from all sources) and any chargeable gains for the period covered by the return and to calculate the tax due. For employees the information required will include details of expenses payments and benefits (except those covered by a dispensation), as well as wages and salaries. Employers will be required to provide all employees with details of expenses payments and benefits to enable them to complete tax returns if they get them.

### How will the changes be brought in

9.13 The Inland Revenue have existing powers to require taxpayers to fully complete their returns, but the new obligations on employers have required legislative changes mainly by changes to the PAYE Regulations. There are also minor changes in the Taxes Management Act 1970 and the Income and Corporation Taxes Act 1988.

### Time at which the changes apply

#### *Section 106(2) FA 1995*

9.14 The changes described in *paras 9.15 to 9.24* will apply to payments made, or benefits provided on or after **6 April 1996**.

### *Changes to PAYE Regulations*

9.15 For tax year 1996/7 onwards employers will have to:

- send P11Ds into the Revenue by 6 July;
- also report expenses payments and benefits where they arrange the provision through third parties;
- show the cash equivalent of any benefits;
- copy the information on the P11D to the employee by 6 July;
- give the P60 to the employee by 31 May.

- 9.16 There will also be a new obligation on third parties making expenses payments and benefits to employees where the direct employer is not responsible for reporting them on form P11D. The third party will have to provide written details to the employee of the expenses payments and benefits by 6 July following the tax year in which they are paid or provided. And, where benefits are provided, the cash equivalent has to be stated.
- 9.17 Regulations have been laid amending the PAYE regulations to cover these and other changes. The changes will be covered in detail in a booklet which will be issued in July 1995.

### *Changes to the Taxes Management Act 1970*

#### **Section 15**

- 9.18 **Section 15** is a general information-seeking power enabling the Inland Revenue to require employers and third parties to provide details about expenses payments and benefits in kind provided to employees.

#### **Three minor changes are required to facilitate Self Assessment**

##### **Section 15(5)(b) and (9)(b)**

- 9.19 The Inland Revenue will be able to ask the employer to provide information about expenses payments made to, and benefits provided for, his employees by another person where the employer has arranged them.

##### **Section 15(9)(a) and 10(a)**

- 9.20 In addition the Inland Revenue will be able to require returns under **Section 15** to include the cash equivalent for each benefit in kind.

##### **Section 15(10)**

- 9.21 Finally, the Inland Revenue will be able to require third parties to return details of expenses payments as well as benefits. (The existing S.15 TMA 1970 only requires details of benefits.)

### *Changes to the Income and Corporation Taxes Act 1988*

#### **Section 205 ICTA 1988**

- 9.22 S.205 ICTA 1988 currently provides that assessments need not be made in the large number of cases where the income tax deducted under PAYE for any tax year is the correct amount for that year. But it also provides that an assessment should be made if the taxpayer so requires.

#### **Two consequential changes are required for Self Assessment**

##### **Section 205(1) and (3) ICTA 1988**

- 9.23 The present reference to an "assessment under Schedule E" is replaced by a reference to 'an assessment'. This is because in Self Assessment the vast majority of assessments will be based on total income.

**Section 205(4) ICTA 1988**

9.24 At present a taxpayer has a time limit of 5 years from the end of the relevant tax year in which to require an assessment to be made. This time limit is increased to 5 years 7 months for Self Assessment. (Under Self Assessment the equivalent of 'requiring an assessment' is requiring the Inland Revenue to issue a personal return so that the taxpayer can self-assess.)

*Conversion table*

TMA		FA 95
<i>Section 15</i>	as substituted by	Section 106(1) FA 1995
ICTA		
<i>Section 205</i> S.206 ICTA 1988	as substituted by consequential amendments	Section 111(1) FA 1995 Section 111(2) FA 1995

Self Assessment for trustees, personal representatives and beneficiaries of estates

*Self Assessment for trustees*

**Self Assessment procedures will apply**

**Section 8A**

- 9.25 Trustees are responsible for making a return of any income, profits or gains arising to a trust, and for paying any income tax or capital gains tax that is due.
- 9.26 All the 'process now-check later' procedures of Self Assessment will apply to trustees. For example, the trustees' return (*Section 8A*) will include a self-assessment which may be subject to repair and enquiry in the normal way. And the same fixed time scale for filing the return and for the payment of tax will apply. Most of these procedures apply automatically to trustees through *Section 9* without the need for additional legislation. But special considerations arise where there is more than one liable trustee to a settlement.
- 9.27 It should also be noted that the return required from trustees may seek information relevant to the tax liabilities of third parties, for example the settlor and beneficiaries of the trust.

**Settlements with more than one liable trustee**

9.28 Where there is more than one trustee to a settlement they are jointly liable for the tax due on the income or chargeable gains arising. Therefore, in law, any one of the trustees could be held liable for the full amount of any tax due. But in practice, trustees usually arrange for one of their number, the '**principal acting trustee**', to deal with the Inland Revenue on their behalf.

## **Under Self assessment any 'relevant trustee' may act on behalf of the trustees**

### ***Section 107A(1)***

9.29 Under Self Assessment any 'relevant trustee' will be able to fulfil the tax obligations of the trustees as a whole simply by taking the appropriate action. This will allow the principal acting trustee to take responsibility for notifying chargeability, for making any return, or for dealing with any enquiry.

## **And the Revenue may take recovery action against any 'relevant trustee'**

### ***Section 107A(2) and (4)***

9.30 Conversely, if the principal acting trustee fails to meet any tax obligations the Revenue may recover any tax, interest, surcharge or penalties due from any other 'relevant trustee'.

## **But no penalty or surcharge may be sought from a person who did not become a 'relevant trustee' until after the penalty or surcharge arose**

### ***Section 107A(3)***

9.31 It may be that a person does not become a trustee until after a penalty or surcharge has arisen. In such cases any recovery proceedings against the new trustee will be limited to any tax, or interest on tax, outstanding, but not any surcharge or penalty (or interest on unpaid surcharge or penalty).

## **Definition of 'relevant trustee'**

### ***Section 7(9) and 118***

9.32 In relation to income a 'relevant trustee' is a person **who is a trustee at the time the income arises, or who becomes a trustee subsequently.**

In relation to chargeable gains a 'relevant trustee' is a person **who is a trustee in the tax year in which the chargeable gains accrue, or who becomes a trustee subsequently.**

9.33 These allow existing tax obligations to pass to new trustees following any changes in bodies of trustees, for example at the death, resignation or retirement of a trustee.

## **Time at which the new rules apply**

### ***Section 103(7) FA 1995***

9.34 The rules for 'relevant trustees' first apply

- for income tax and capital gains tax **from 1996/97;**

## Conversion table

TMA 1988		FA 94 & 95
<i>Section 7(2)</i>	as substituted by	para 1(1), Schedule 19 FA 1994 and Section 103(1) FA 1995
<i>Section 7(9)</i>	as inserted by	Section 103(2) FA 1995
<i>Section 8A(1)</i>	as substituted by	Section 178(2) FA 1994 and Section 103(3) FA 1995
<i>Section 8A(5)</i>	as inserted by	Section 103(4) FA 1995
<i>Section 107A</i>	as inserted by	Section 103(5) FA 1995
<i>Section 118</i>	as amended by	
<i>Section 90(6) FA 1995</i>		
<b>TCGA 1992</b>		
<i>Section 65(1) &amp; (2)</i>	as substituted by	Section 114 FA 1995

## *Self Assessment for Personal Representatives and the Beneficiaries of Estates*

### Introduction

9.35 The tax arising on the income from the estate of a deceased person is accounted for in two ways:

- the **Personal Representatives** responsible for the administration of the estate must deduct tax from all estate income at the basic rate (or at the lower rate for dividend income),
- but that income is then attributed to the **beneficiaries with an interest in the estate**. In the case of a UK estate this income is **taxed income**, with an associated tax credit.

9.36 This procedure means that a beneficiary who is a higher rate taxpayer will be liable to further tax on their share of income from the estate. Other beneficiaries may have no further liability, or may be entitled to a repayment of part, or all, of the associated tax credit, depending on the circumstances.

9.37 In general terms all the 'process now-check later' procedures of Self Assessment will apply to both personal representatives, and to the beneficiaries of estates, without the need for changes to the existing legislation. But special considerations arise in the context of **beneficiaries with an interest in the residue of an estate**.

### Self Assessment for Residuary Beneficiaries

9.38 The 'residue' of a deceased person's estate is the amount remaining after the payment of any debts, specific legacies and other outgoings. Any income of the residue is attributed to the beneficiaries with interest in that residue.

- 9.39 The beneficiaries are initially taxed on any payments that are made to them as payments of income from the estate. But the existing rules require that the final liability on the income from the estate can only be determined at completion. The whole amount of any such income is totalled up and spread rateably back across the entire period of administration. Where appropriate fresh assessments must be made, or existing assessments revised.
- 9.40 The current rules for income spreading are clearly incompatible with the general principles of Self Assessment. Therefore, under Self Assessment the income will be taxed in the year of receipt. Any amounts outstanding when the administration period ends will be treated as paid at that time, regardless of the period in which they actually arose.

### **Time at which the new rules apply**

#### ***Paras 2(2), 3(3), 4(3) and 5(2) Schedule 18 FA 1995***

9.41 The new rules apply to

- any payments made on or after 6 April 1995;
- for payments treated as made at the completion of a period of administration, to any completion on or after 6 April 1995.

### **Limited Interests**

#### ***Para 2, Schedule 18 FA 1995***

- 9.42 Beneficiaries, such as life tenants, who are entitled to have the income of the estate paid to them are said to have a 'limited interest' in the residue. Under Self assessment they will be liable to tax on payments made to them out of an estate. Any such payments will be treated as payments net of tax at the appropriate rate (either the basic rate, or for payments out of dividends, the lower rate). This means that beneficiaries who are non-taxpayers, or lower rate taxpayers, will be entitled to a repayment of some or all of the tax. Higher rate taxpayers will have additional tax to pay.
- 9.43 If, on completion of the estate, any amounts to which the beneficiary is entitled remain unpaid they will be deemed to be income of the year of assessment in which the date of completion falls.

### **Absolute Interests**

#### ***Paras 3 & 4, Schedule 18 FA 1995***

- 9.44 Beneficiaries who are entitled to a share of **the whole or part of the income and capital of the residue** are said to have an 'absolute interest' in the residue. Under Self assessment they will be liable to tax on payments made to them out of the estate. Any such payments will be treated as income for the year of payment. And again any such payments will be treated as payments net of tax at the appropriate rate.
- 9.45 But any such payments will only be treated as income to the extent that they do not exceed the 'aggregated income entitlement' of the beneficiary at the time the payment is made. The 'aggregated income entitlement' is the cumulative share of the estate income, for all years up to and including the year of payment, to which the beneficiary is entitled whether or not that share has actually been paid out. In other words the beneficiary is liable to tax on the lesser of the cumulative share of estate income, or the amounts actually paid.

- 9.46 At the end of the administration any part of the beneficiary's 'aggregated income entitlement' that remains unpaid will be treated as paid immediately before the end of the administration period. So beneficiaries will be charged on the whole of their share of the estate income even if it has not been paid to them when administration is completed.
- 9.47 If, when arriving at the beneficiary's share of estate income there is an excess of expenses over income that excess will be carried forward and deducted in the following year. Similarly if the 'benefits received' from the estate fall short of the beneficiary's estate income that income is reduced by the shortfall in the year in which the administration ends. Benefits received in this context include sums paid on completion of the administration.

### Successive Interests in Residue

#### *Para 5, Schedule 18*

- 9.48 'Successive interests' in residue can be held where an interest is disclaimed or varied by the original beneficiary. The subsequent interest is treated as having always existed and held by the beneficiary entitled to receive the payment *when it is made*. So, if a beneficiary receives a payment for a period before his or her interest came into being it will be treated as his or her income. Payments made in respect of an interest which has ceased will likewise be treated as the income of the person entitled to them. The result is that each beneficiary is assessed only on the income paid to them.
- 9.49 Different rules apply where a life interest is terminated by death. Any sums paid after the beneficiary has died are treated as his income for the year of assessment in which the interest ceased.

### Statement by Personal Representative

#### *Para 6, Schedule 18 FA 1995*

- 9.50 Each beneficiary may request a statement from the personal representatives of the amounts deemed to be paid as income and the tax deducted, distinguishing between tax at lower and basic rates. The personal representatives are required to provide any such statement if one is requested.

### *Conversion table*

#### **ICTA 1988**

**Section 695**  
**Section 696**  
**Section 697**  
**Section 698(1A), (1B) and (2)**  
**Section 700(5), (5) and (7)**  
 Section 701(14) ICTA 1988

as amended by  
 as amended by  
 as amended by  
 as substituted by  
 as inserted by  
 as repealed by

#### **FA 95**

para 2, Schedule 18 FA 1995  
 para 3, Schedule 18 FA 1995  
 para 4, Schedule 18 FA 1995  
 para 5, Schedule 18 FA 1995  
 para 6, Schedule 18 FA 1995  
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These notes are for guidance only and reflect the tax position at the time of writing. It should be borne in mind that the notes are not binding in law and in a particular case there may be special circumstances that will need to be taken into account.

It should also be noted that there will be further legislation for Self Assessment in the Finance Act 1996. This legislation may modify the operation of the rules described in this guide.

These notes do not affect any right of appeal a taxpayer may have.

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