

Summary: Intervention & Options

Department /Agency: HMRC	Title: Interest-Working Towards a Harmonised Regime	
Stage: Consultation	Version: 1	Date: 19 June 2008
Related Publications: Consultation Document: Interest – Working Towards a Harmonised Regime		

Available to view or download at:

<http://www.hmrc.gov.uk/consultations>

Contact for enquiries: Bob Horwill

Telephone: 020 7147 2447

What is the problem under consideration? Why is government intervention necessary?

The rules governing the charging of interest on late payments and paying out of interest on overpayments of taxes and duties are set out in legislation. They have developed over a number of years as each tax or duty has been introduced or has evolved. Although the overarching interest rules and the legislative framework are similar across the taxes and duties where interest applies, there are a number of differences. These differences add unnecessary complexity to the tax system for taxpayers, their advisers and for HM Revenue & Customs (HMRC).

What are the policy objectives and the intended effects?

To establish a balanced and more effective interest regime based on the principles of recompense, fairness and simplicity. Harmonisation of interest will bring benefits for taxpayers, their advisers and HMRC who will have a clearer understanding of interest rules and their respective obligations. The focus is on simplifying and harmonising how HMRC charge and pay interest across tax regimes, rather than on making any changes to how the underlying tax regimes operate.

What policy options have been considered? Please justify any preferred option.

- 1) Preserve the status quo.
 - 2) Align rates for charging and paying interest only for those taxes and duties where HMRC currently charge and pay interest.
 - 3) Charge and pay interest consistently and automatically on all taxes and duties.
- Option 3 is our preferred option because it will enable us to achieve all our policy aims.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects? Any reforms would be subject to post – implementation review once they have bedded in (typically 2 -3 years). The final Impact Assessment will contain further analysis arising in the course of the consultation.

Ministerial Sign-off For Consultation Stage Impact Assessments:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister: Jane Kennedy

.....Date: 19 June 2008

Summary: Analysis & Evidence

Policy Option: 1	Description: Preserve the status quo
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COSTS	ANNUAL COSTS	Description and scale of key monetised costs by 'main affected groups' If the decision is made to retain the present interest regime no change will be implemented.		
	One-off (Transition) Yrs			
	£ Nil			
	Average Annual Cost (excluding one-off)			
	£ Nil	Total Cost (PV)	£ Nil	
Other key non-monetised costs by 'main affected groups' None				

BENEFITS	ANNUAL BENEFITS	Description and scale of key monetised benefits by 'main affected groups' None		
	One-off Yrs			
	£ Nil			
	Average Annual Benefit (excluding one-off)			
	£ Nil	Total Benefit (PV)	£ Nil	
Other key non-monetised benefits by 'main affected groups' None				

Key Assumptions/Sensitivities/Risks The present interest regime needs to be revisited as there are doubts whether it fully meets the principles upon which an effective interest regime should be based. The "status quo" option does not introduce any new costs or benefits, but it represents a missed opportunity to achieve greater fairness and simplicity.

Price Base Year	Time Period Years	Net Benefit Range (NPV) £	NET BENEFIT (NPV Best estimate) £ Nil
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What is the geographic coverage of the policy/option?	United Kingdom			
On what date will the policy be implemented?	N/A			
Which organisation(s) will enforce the policy?	HMRC			
What is the total annual cost of enforcement for these organisations?	£ No added cost			
Does enforcement comply with Hampton principles?	Yes			
Will implementation go beyond minimum EU requirements?	No			
What is the value of the proposed offsetting measure per year?	£ N/A			
What is the value of changes in greenhouse gas emissions?	£ N/A			
Will the proposal have a significant impact on competition?	No			
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	No	No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices)		(Increase - Decrease)	
Increase of	£ Nil	Decrease of	£ Nil
		Net Impact	£ NIL

Key: Annual costs and benefits: Constant Prices (Net) Present Value

Summary: Analysis & Evidence

Policy Option: 2

Description: Align rates for charging and paying interest only for those taxes and duties where HMRC are currently charging and paying interest

COSTS	ANNUAL COSTS		Description and scale of key monetised costs by 'main affected groups' There are no known additional compliance costs which taxpayers would incur in complying with their tax and legal obligations. The financial impact on taxpayers and HMRC depends on the levels of interest charged and paid, and the divergence between the two. Work is continuing to quantify specific impacts.
	One-off (Transition)	Yrs	
	£ Negligible		
	Average Annual Cost (excluding one-off)		
	£ Not known		Total Cost (PV) £
<p>Other key non-monetised costs by 'main affected groups' There may be some cost to the taxpayer in becoming familiar with a new regime, but this is expected to be negligible and will be offset by a more simplified and streamlined process for the calculation and application of interest. This should improve cost effectiveness and provide saving in resource time.</p>			

BENEFITS	ANNUAL BENEFITS		Description and scale of key monetised benefits by 'main affected groups' As above, the financial impact on individual taxpayers and HMRC would depend on the levels of interest charged and paid. Greater harmonisation of the interest charging and paying rules could bring benefits for taxpayers, their advisers and for the administration of the tax system.
	One-off	Yrs	
	£ Nil		
	Average Annual Benefit (excluding one-off)		
	£ Not known		Total Benefit (PV) £
<p>Other key non-monetised benefits by 'main affected groups' The simplification of the interest regime will provide taxpayers/others with a fairer system which is more comprehensible and manageable, and will enable them to spend less time understanding how it works. A fairer regime will ultimately benefit all taxpayers, in terms of recompense to the UK Exchequer from those who default on their obligations.</p>			

Key Assumptions/Sensitivities/Risks The policy objective is to deliver a more efficient regime based on recompense, fairness and simplicity (as outlined in chapter 3 of the consultation document).

Price Base Year	Time Period Years	Net Benefit Range (NPV) £	NET BENEFIT (NPV Best estimate) £
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What is the geographic coverage of the policy/option?			United Kingdom		
On what date will the policy be implemented?			N/K		
Which organisation(s) will enforce the policy?			HMRC		
What is the total annual cost of enforcement for these organisations?			£ No added cost		
Does enforcement comply with Hampton principles?			Yes		
Will implementation go beyond minimum EU requirements?			No		
What is the value of the proposed offsetting measure per year?			£ N/A		
What is the value of changes in greenhouse gas emissions?			£ N/A		
Will the proposal have a significant impact on competition?			No		
Annual cost (£-£) per organisation (excluding one-off)		Micro	Small	Medium	Large
Are any of these organisations exempt?		No	No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices)			(Increase - Decrease)		
Increase of	£ Nil	Decrease of	£ Negligible	Net Impact	£ Negligible

Key: Annual costs and benefits: Constant Prices (Net) Present Value

Summary: Analysis & Evidence

Policy Option: 3
(preferred option)

Description: Charge and pay interest consistently and automatically on all taxes and duties

COSTS	ANNUAL COSTS		Description and scale of key monetised costs by 'main affected groups' Taxpayers are unlikely to incur any significant administrative costs as a result of this reform. The cost to HMRC to extend interest to all taxes is very much dependant on IT requirements, which are still under consideration with IT partners.
	One-off (Transition)	Yrs	
	£ Not known	0	
	Average Annual Cost (excluding one-off)		
	£ Not known		Total Cost (PV) £
<p>Other key non-monetised benefits by 'main affected groups' There may be a small (negligible) time cost to the taxpayer in becoming familiar with a new regime. The proposed simplification and extension of the interest process should provide some HMRC staff cost savings through the streamlining of processes, which may be balanced by additional resource needs required to cover queries if interest is extended to new areas/taxes.</p>			

BENEFITS	ANNUAL BENEFITS		Description and scale of key monetised benefits by 'main affected groups' Simplification/extension of interest to all taxes provides taxpayers with a manageable interest regime with potential for greater recompense.
	One-off	Yrs	
	£ Not known		
	Average Annual Benefit (excluding one-off)		
	£ Not known		Total Benefit (PV) £
<p>Other key non-monetised benefits by 'main affected groups' Simplification and extension of interest to all regimes will provide a level playing field between those who pay and those who do not to pay. A fairer regime will ultimately benefit all taxpayers, in terms of recompense to the UK Exchequer from those who default on their obligations.</p>			

Key Assumptions/Sensitivities/Risks In addition to administrative effects, the amount of interest charged may itself change if interest is extended to other tax regimes such as in year-PAYE. Work is continuing to quantify the likely impacts. It is also expected that where interest is extended to other tax regimes HMRC will continue to compute the interest due from taxpayers.

Price Base Year	Time Period Years	Net Benefit Range (NPV) £	NET BENEFIT (NPV Best estimate) £
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What is the geographic coverage of the policy/option?		United Kingdom	
On what date will the policy be implemented?		N/K	
Which organisation(s) will enforce the policy?		HMRC	
What is the total annual cost of enforcement for these organisations?		£ Low	
Does enforcement comply with Hampton principles?		Yes	
Will implementation go beyond minimum EU requirements?		No	
What is the value of the proposed offsetting measure per year?		£ N/A	
What is the value of changes in greenhouse gas emissions?		£	
Will the proposal have a significant impact on competition?		No	
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium Large
Are any of these organisations exempt?	No	No	N/A N/A

Impact on Admin Burdens Baseline (2005 Prices)			(Increase - Decrease)
Increase of	£ Nil	Decrease of	£ Negligible Net Impact £ Negligible

Key: Annual costs and benefits: Constant Prices (Net) Present Value

1) Background

1.1. The rules governing all interest that HM Revenue and Customs (HMRC) charges on late payments and pays out on overpayments are set out in legislation. They have developed over a number of years as each tax or duty has been introduced or has evolved.

1.2. Although the overarching interest rules and the legislative framework are similar across the taxes where interest applies, there are anomalies and inconsistencies which need to be addressed. All taxes¹ and duties administered by HMRC are in scope for this review, with the exception of tax credits, child benefit and customs duties.

1.3. The consultation document considers a number of areas where greater harmonisation of the interest charging and paying rules could bring benefits for taxpayers, their advisers and for the administration of the tax system. The aim is to establish a balanced and more effective interest regime based on the principles of recompense, fairness and simplicity.

1.4. The focus of the consultation is on simplifying and harmonising how HMRC charge and pay interest across tax regimes, rather than on making any changes to how the underlying tax regimes operate.

2) The policy options

The policy options presented in this section of this impact assessment should also be considered in the context of a separate consultation and associated impact assessment on a structured approach to late payment published alongside this consultation.

2.1. Option one - Preserve the status quo

i) Under the existing interest regime there are currently nine different formulas in use generating interest rates ranging from 4% to 7.5% charged on late payments and from 2.75% to 5.75% applied to overpayments of tax.

ii) These different rates combined with the fact that interest is not consistently charged and paid across taxes add complexity to the tax system. This complexity has extra cost and resource implications for taxpayers, their advisers, and for HMRC as it does not enable taxpayers to identify easily the consequences of paying late.

2.2. Option two - Align rates for charging and paying interest only for those taxes and duties where HMRC are currently charging and paying interest

i) This option would simplify the existing regime for charging and paying interest for those taxes where it already exists by aligning the rates charged and paid. For those taxes the revised interest regime would be based on the principles of recompense, fairness and simplicity, with one common rate of interest for late payment and another for all overpayments, although not necessarily the same rate. At the other end of the scale this

¹ As in the consultation document, with the exception of Customs duties, "taxes" should be taken in this document to include all the taxes, duties and national insurance contributions for which HMRC is responsible. Taxpayer should be taken to include anyone paying such taxes as well as those paying tax on behalf of another person.

would mean a fuller alignment along the lines of the points covered at paragraph 3.4 (below).

ii) There should be benefits for taxpayers through easier understanding of the basis on which interest is charged and paid out on those taxes and duties where it currently applies.

iii) Significant IT changes would not be expected which would mean lower IT costs for HMRC.

2.3. Option three - Charge and pay interest consistently and automatically on all taxes and duties

i) This option follows the same principles outlined at option 2 above and builds on the changes suggested there. Under this option the interest regime would be extended to include all other taxes and duties where no interest is currently charged or paid as well as aligning the underlying rules for interest. This would ensure that interest would be applied consistently to all late payments and repayments of tax.

ii) Implementing this option would lead to a fairer more comprehensive interest regime. HMRC are working with their IT partners on the likely cost of making the IT changes and this will ultimately influence how this option is taken forward.

3) Policy issues to be addressed

3.1. The policy underlying this reform is to create an effective interest regime that is based on recompense, fairness and simplicity. This will enable taxpayers to better understand the interest consequences of their payment decisions.

3.2. The consultation seeks to engage with taxpayers, their advisers and representative bodies to decide how the new interest regime should be developed and applied for the future. It is important that the final regime is simple, fair to those that pay on time, and provides both the Exchequer and the taxpayer with recompense for tax paid late or overpayments of tax. Interest is not a penalty but is charged or paid as recompense to whichever party has not had use of money over a period of time.

3.3. Chapters 4 and 5 of the consultation document discuss in detail a number of issues regarding the construction of an interest regime and it is particularly in these areas that we will engage with taxpayers and representatives to find solutions that achieve the best balance of the design principles. These chapters include discussion points about the way interest is presently charged, how the rates are calculated (including debate about the 'rounding' process), the differentials between late payment rates and overpayment rates, and considers how interest might be charged on late payments under the Pay As You Earn system using the three approaches identified in the 'Meeting the obligations to file returns and pay tax on time' consultation document published alongside this document..

3.4. To enable an appropriate decision to be made views are sought about various aspects of interest including whether it should be:

- charged automatically on all taxes and repaid on overpaid taxes
- charged automatically on the same basis;
- calculated by reference to (and hence track) a single external interest rate;

- charged at one rate for late payment and paid at one rate for overpayments; and
- set at regular intervals to ensure a balance between stability and recompense.

3.5. Chapter 6 of the consultation document looks at how the principles of recompense, fairness and simplicity could be reflected in the rates themselves. This chapter acknowledges that, in setting the rate or rates for a revised interest regime careful consideration of the existing Quarterly Instalment Payments (QIPs) position and the dynamics behind that position may need to be carefully factored into the revised rates of interest.

3.6. The responses generated by the consultation will be used to inform decisions and help shape any new the interest regime. HMRC will also continue to work with its analysts alongside the consultation to gather evidence to support the final policy recommendations.

4) Costs & benefits

4.1. Compared with the status quo, the proposed reforms offer a range of benefits to both taxpayers and HMRC. The consultation exercise seeks views from our taxpayers (and their advisers) on the various options. In particular views are sought on how the desired benefits might be realised at minimum cost.

Costs & benefits to businesses and their advisers

4.2. The main administrative benefits from a business perspective are:

- greater fairness – because the interest rate charged will be more consistent across different taxes and taxpayers
- greater simplicity – making calculations easier to understand and apply
- greater certainty – simplifying language and harmonising rates makes it easier for taxpayers to understand the consequences of their decisions and actions.

4.3. These reforms are not expected to introduce any significant administrative costs, although a small amount of time may be required as taxpayers and their advisers familiarise themselves with any new rules.

Costs & benefits to HMRC

4.4. HMRC would need to modify its systems for calculating interest and notifying taxpayers of interest charged and paid out. This would entail an upfront IT cost, with associated staff training. Subsequently, the reduced complexity will enable HMRC to offer a more streamlined and efficient service.

5) Financial impacts

5.1. The policy objective is to establish a balanced and more effective interest regime based on the principles of recompense, fairness and simplicity. However, individual businesses and taxpayers may see the rate applicable to them change and because of this there will likely be winners and losers when the rates are set. A full analysis of the likely effects is under development, but in simplistic terms:

- businesses that currently pay a high (above average) interest rate, may be charged a lower rate if rates are harmonised; and

- businesses that currently pay a low (below average) interest rate may be charged a higher rate if rates are harmonised.

5.2. In both cases, the result is a fairer system that treats all businesses and taxpayers equally. It also ensures that those who default on their tax obligations pay recompense to the Exchequer. Similarly for those taxpayers who overpay, the rate of interest paid reflects recompense from the Exchequer.

Quantifying the expected costs and benefits

5.3. HMRC is continuing to work with its analysts and information technology partners to measure the likely impacts of aligning the interest regime. This work, together with feedback from the consultation, will inform the way forward, with a full impact assessment (including quantified costs and benefits) published in due course for the preferred option(s).

6) Administrative burdens

6.1. Within the broader category of administrative compliance costs, HMRC monitors one element in particular. The “administrative burden” is specifically defined as “the recurring cost and time necessarily incurred by efficient and compliant businesses in sending information to HMRC or a third party”. It includes obligations such as completing tax returns, making tax payments and complying with audits and inspections. HMRC has specific targets to reduce the administrative burden on business, and all impact assessments include an estimate of the expected effect.

6.2. In this case, interest charges are normally incurred (or received) only by those who have not paid the correct amount of tax initially. This falls outside the above definition of “administrative burden” and as such, it appears that there is unlikely to be any significant impact from this measure.

6.3. Throughout the consultation work will continue to monitor and quantify the likely costs and benefits more generally as the options and the likely impacts are refined, so that the policy objectives are fully achieved.

7) Specific impact tests

7.1. The full range of impact tests shown in the checklist below have been applied. In particular the following impacts were considered.

Competition Assessment

7.2. The objective of this consultation is to create an effective interest regime based on recompense, fairness and simplicity. Such a regime would reduce the chance of different businesses paying different rates. As such, this will present a more level playing field for businesses to operate on. By applying the same rate for late payment the interest regime would create a level playing field between taxpayers who pay at different times.

Small Firms Impact Test

7.3. The proposed changes in the interest regime will affect all businesses due to the possible changes in the way rates of interest are charged as a result of non payment or late payment. The introduction of a simpler process should provide business with greater clarity and more transparency into HMRC’s interest regime. The simplification of interest, while benefiting all types of business, should particularly help small business function more effectively by making it more straightforward for them to understand their responsibilities.

7.4. It is not expected that that there will be any impact on the other areas listed in the checklist. Completion of analysis and consultation will enable the impact tests to be firmed up but presently it is not expected there will be any significant effect but this early conclusion is subject to comments received during the consultation.

Specific Impact Tests: Checklist

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	Yes	No
Small Firms Impact Test	Yes	No
Legal Aid	No	No
Sustainable Development	No	No
Carbon Assessment	No	No
Other Environment	No	No
Health Impact Assessment	No	No
Race Equality	No	No
Disability Equality	No	No
Gender Equality	No	No
Human Rights	No	No
Rural Proofing	No	No