

Changes to VAT penalties (Lecture B1410 – 20.47 minutes)

Changes to VAT penalties

The new filing and payment regime replaces the old default surcharge regime, and applies for VAT for accounting periods beginning on or after 1 January 2023.

There are no transitional rules when moving from the default surcharge to the new regime so all traders will start with a clean slate under the new regime.

This same regime is due to be rolled out for direct taxes on a graduated basis from April 2026 so as to tie with MTD for income tax.

Late filing regime

After reaching a 'points' threshold, there is a late submission penalty of £200 for each late submission.

Taxpayers receive one point for each late submission and will be notified each time a point is awarded. Whilst below the 'points' threshold, the points have a two-year shelf life, after which time they effectively expire.

The 'points' threshold varies, and depends on the submission frequency of the trader:

<u>Returns submitted</u>	<u>Points</u>
Annually	2
Quarterly (including MTD IT)	4
Monthly	5

So for quarterly submissions, penalties will apply after four late quarterly returns. At this time, four points will have been awarded and with that fourth point will come a £200 penalty.

Once the 'points' threshold is reached, the two-year expiry window for points becomes irrelevant. A £200 penalty will be charged for each late return until the taxpayer has filed returns on time for:

- 24 months where annual submissions are made;
- 12 months where quarterly submissions are made;
- 6 months where monthly submissions are made.

At this time, the points will be reset to zero but only if all returns for the last 24 months have actually been submitted. You cannot benefit from the reset if you have earlier returns still outstanding.

HMRC have a time limit for levying a point which is:

- 48 weeks for annual submissions;
- 11 weeks for quarterly submissions;

- 2 weeks for monthly submissions.

This will be extended to 12 months when HMRC were unaware of a taxpayer's submission obligations.

Reasonable excuse for late filing

Taxpayer's can appeal against HMRC's decision to issue a penalty point, or against a penalty charged once you have reached the 'points' threshold, provided there is a reasonable excuse for late filing.

Reasonable excuse could include:

- Computer breakdown before or during the preparation of the VAT return;
- Illness of the only person able to prepare/submit the VAT return but the taxpayer must take reasonable steps to get someone else in cases of prolonged illness;
- Loss of the only person who can prepare the VAT return leaves at short notice;
- Unexpected cash crisis such as the unexpected withdrawal of bank overdraft, non-payment by a regular payer, burglary or act of God;
- Loss of records where they are stolen or destroyed.

All of these excuses could apply for late payment as well as late filing.

Late payment regime

Under the new late payment regime, interest will always be charged on late payments at base rate plus 2.5%.

In addition to the late payment interest, the taxpayer may be liable to two late payment penalties.

Provided that the tax is paid within 15 days of the payment deadline, additional penalties are avoided. After that, a first penalty will be payable as follows:

- Late payment between Day 16 to 30: penalty is 2% of the outstanding tax at Day 15;
- If the tax is paid more than 30 days late, then a further sum is due calculated as 2% of the outstanding tax at Day 30.

In addition, there is a second penalty representing daily interest calculated by applying a 4% annualised rate on outstanding tax due after 30 days.

As with the filing regime, taxpayers with a reasonable excuse or special circumstances can apply to have the penalties cancelled.

Time to pay arrangement

Under a Time To Pay (TTP) arrangement, the taxpayer is treated as if they paid the tax on the date of the TTP agreement. Consequently, from this date penalties cease to accrue but only if the TTP terms are honoured.

If a TTP arrangement is agreed during days:

0 to 15	No penalties will be payable;
16 to 30	Only the initial 2% penalty will apply;
> 30 days	First penalty will increase to 4% but the second penalty will stop accruing at the date the TTP is agreed.

Note that late payment interest cannot be avoided and will continue to be charged.

Example 1

VAT return to 31 August 2023 shows a VAT liability of £10,000 and the taxpayer fails to pay this by the due date of 7 October 2023.

The taxpayer approaches HMRC to agree a TTP on 18 October 2023 which is Day 11. Having agreed the terms, the taxpayer honours those terms.

For the purposes of the first and second penalties the taxpayer is deemed to have settled the VAT on 18 October 2023. No penalties are due as the tax is deemed to have been settled by Day 15.

Interest will continue to accrue on any outstanding amounts.

Example 2

What if the taxpayer approaches HMRC to agree a TTP on 27 October 2023 which is Day 20 and subsequently honours the terms agreed?

For the purposes of the first and second penalties the taxpayer is deemed to have settled the VAT on 27 October 2023, which is after Day 15 but before Day 30. Consequently, the initial penalty of 2% is charged but no further penalties are payable (but see light touch approach below).

Interest will continue to accrue on any outstanding amounts.

Example 3

What if the taxpayer approaches HMRC to agree a TTP on 10 November 2023 which is Day 34 and subsequently honours the terms agreed?

For the purposes of the first and second penalties the taxpayer is deemed to have settled the VAT on 10 November 2023 which is after Day 30.

Consequently, the first penalty of 4% is charged (2% + 2%) and the second penalty will run for 4 days calculated at 4% per annum.

Interest will continue to accrue on any outstanding amounts.

Light touch approach

As this is a new system and taxpayers may struggle to contact HMRC within 15 days to agree a TTP, HMRC are adopting a light touch approach.

This will apply to the initial 2% penalty for the first year of operation of the new system only.

Where a taxpayer is seen to be doing their best to comply, HMRC will not assess the first 2% penalty for the 16-to-30-day period. This effectively allows a taxpayer 30 days to agree a TTP arrangement.

However, if a taxpayer has not agreed a TTP by Day 30, the first 2% penalty will be fully charged as well as the 2% of tax outstanding at Day 30.

Reviews and appeals

HMRC will tell you when you have a late submission point or a £200 penalty in a penalty decision letter, which will also offer you a review with HMRC.

Where a taxpayer has a reasonable excuse, it could be worth a review. This can be requested through their online account.

If the review is unsuccessful, the taxpayer could appeal to the First Tier Tribunal. However, given the level of the penalty, this is unlikely to be worth it for late filing.

Created from the seminar by Dean Wootten