

HMRC – Voluntary restitution (Lecture P1410 – 10.59 minutes)

This article will consider the position where HMRC invite a taxpayer to make “voluntary restitution”.

What is voluntary restitution?

Voluntary restitution is the payment of tax or National Insurance Contributions (NIC) where HMRC do not have a legal ability to assess the tax or NIC.

When can HMRC seek voluntary restitution?

HMRC will usually be able to rely on an offence by a taxpayer to recover tax or NICs that have been “lost”. This can include where a taxpayer has failed to notify liability, or where a taxpayer has submitted an incorrect tax return and HMRC have issued an enquiry notice within the statutory timeframe for doing so.

However, that is not always the case. There can be instances where there has been a loss of tax or NICs, but HMRC are not able to legally recover those amounts. This can include where:

- the taxpayer had a reasonable excuse for the failure to notify liability;
- the taxpayer successfully demonstrates that his incorrect returns (or accounts) were submitted innocently for periods where the filing date for the return is on or before 31 March 2009;
- the taxpayer successfully demonstrates that, for periods beginning on or after 1 April 2008 where the filing date for the return is on or after 1 April 2009, that the inaccuracy in the return(s) arose despite the taxpayer taking reasonable care;
- the taxpayer has died and HMRC’s right to assess is limited (by Section 40(2), Taxes Management Act 1970);
- the taxpayer submitted a return (or accounts) at the proper time but HMRC failed to open an enquiry in time.

Where HMRC are not able to legally recover lost tax or NICs, those amounts, plus related interest and penalties, cannot be assessed, or included in an expected offer to HMRC (under a contract settlement).

HMRC’s position

HMRC’s view is that, that even though they cannot legally recover lost tax or NICs (in the circumstances noted above), they are justified in inviting voluntary restitution on equitable grounds. This position is confirmed in HMRC’s Enquiry Manual (at EM3980). HMRC are appealing to the client’s inner moral compass, or philanthropic nature, to pay tax that is not legally due.

In these circumstances, HMRC will seek the amount of the expected offer, and the irrecoverable tax and NIC with simple interest, but without any penalty.

HMRC officers are told that the invitation to make voluntary restitution should be made only after the maximum penalty that could be charged and HMRC’s policy of abatement (or reduction of type

and quality of disclosure for periods beginning on or after 1 April 2008 where the filing date is on or after 1 April 2009) has been full explained.

HMRC officers are also told that where the taxpayer or personal representative does not agree to make voluntary restitution, it should not be pressed, and any subsequent negotiations should be conducted without reference to the amounts which HMRC cannot legally recover. HMRC acknowledge that any offer in excess of the expected offer will be acceptable.

The client's position

The adviser will need to establish whether HMRC has a legal basis for recovering the tax, etc, that is being sought. This will involve consideration of the client's circumstances, including the relevant assessing time limits, HMRC actions, and the client's behaviour, where appropriate.

When it is determined that HMRC are not able to legally assess tax or NICs, the client will need to consider whether they wish to pay tax (or NICs) in such circumstances. If a client decides to make voluntary restitution to HMRC, they are not obliged to pay interest or a penalty on the relevant tax or NIC. As noted above, HMRC will request the payment of simple interest, but there is not any obligation on the taxpayer to make such payment.

HMRC cannot enforce payment of the irrecoverable tax (or NIC), and the client may decide to make full or partial payment of the tax that HMRC are not able to legally assess. If the client decides not to make voluntary restitution, decides to make only a partial payment, or decides not to pay interest, HMRC cannot take any enforcement action in relation to those amounts.

It is for the client to decide whether they make voluntary restitution to HMRC. I have dealt with numerous instances over the years where the issue of voluntary restitution has arisen and needs to be discussed with the client. Some clients may choose to make a payment, whether in full or part, and others may decide not to make a payment to HMRC. Where a client decides not to make a payment to HMRC, they may, instead, choose to make a donation to a charity of their choice.

Apart from the moral dilemma, a client may decide to make voluntary restitution to HMRC to avoid another tax liability, and associated interest charge, as some taxpayers did a few years ago in relation to the loan charge.

Practical considerations

When advisers are dealing with a voluntary disclosure, or an HMRC enquiry, they need to carefully consider the legal position, and HMRC's ability to assess a particular year. This will, usually, require consideration of the relevant behaviour. Where, for example, the client's deliberate behaviour has resulted in the submission of an incorrect return and an underpayment of tax, the resulting tax liabilities, and associated penalties, should be calculated. It would not be appropriate to submit calculations for six years, and claim careless behaviour, but offering voluntary restitution for earlier years to avoid the imposition of a penalty.

When a case is being settled by a contract, the adviser will need to check that the wording is amended to reflect the inclusion of the voluntary element of the payment to HMRC.

Contributed by Phil Berwick, Director at Berwick Tax