

Sanctions for the late payment of tax

(Lecture B1157 – 10.26 minutes)

As part of its Making Tax Digital (MTD) initiative, the government is proposing to simplify and harmonise the penalty regimes for both the late filing of relevant returns and the late payment of tax.

In response to consultations, the government has published draft legislation to facilitate the introduction of:

- A new “points based” penalty system for the late filing of returns; and
- A new harmonised penalty regime for the late payment of tax.

These notes will look at the new proposals to charge penalties for late tax payments.

The current regime – a quick recap

Penalties apply for both the late filing of self-assessment (SA) returns and late payment of income tax under SA. The current regime has applied since the tax year 2010/11.

The current penalties for the late payment of income tax are:

<u>Degree of lateness</u>	<u>Penalty</u>
0 – 30 days	Nil
31 days – 6 months	5% of the outstanding tax
6 months – 12 months	A further 5% of the outstanding tax
More than 12 months	A further 5% of the outstanding tax

Interest is also charged on unpaid income tax (at the prevailing HMRC interest rate). Late payments on account of income tax will suffer an interest charge but are not subject to the penalty regime.

Late payment penalties must be paid within 30 days of the date the notice assessing the penalty is issued. Interest is charged if penalties are paid late.

Taxpayers who fail to make payments of tax by the due date may enter into an agreed ‘Time To Pay’ (TTP) arrangement with HMRC. Tax payment will then be deferred and no late payment penalties will be charged. The taxpayer will become liable to late payment penalties if the TTP agreement is broken.

There are currently no penalties for late payment of corporation tax. [Provisions for penalties for late paid corporation tax were laid down in Sch 56 FA 2009 but have never been implemented.] There are however penalties where companies fail to make payments (or deliberately understate payments) due under the quarterly payment regime. Interest is charged on any corporation tax paid late.

There is no standalone late payment penalty regime for VAT. Instead the default surcharge regime applies. This is a combined sanction for late submission of VAT returns and late payment of VAT.

The new regime for late tax payments – the background

In July 2018, HMRC published a Policy Paper entitled “Interest Harmonisation and sanctions for late payment”.

The paper lays out the government’s proposals to replace the existing late payment penalties with shiny new ones. The intention is that the new regime will dovetail more comfortably with Making Tax Digital (MTD) by “simplifying and harmonising late payment penalties and interest” and “making the tax administration system clearer and simpler for taxpayers, ensuring that it is as easy as possible for them to comply with their obligations across taxes”. Fine words indeed.

The new system will replace the existing multiple late payment penalty regimes with one harmonised system to apply for income tax, corporation tax and VAT. This will result in increased penalties for companies who pay their corporation tax late, as late payment penalties are not currently charged under the existing CT regime.

The proposals were originally included in Finance Bill 2019 but have since been temporarily shelved. These draft clauses will now reappear in a future Finance Bill. Despite its best intentions, it is not anticipated that the government will be able to roll-out the new system any earlier than April 2021. It is understood that VAT is the designated guinea pig and will have the honour of being the first to be migrated across to the new system. Income tax and corporation tax will follow.

The new late payment penalty rules

Under the new proposals, no late payment penalties will be charged if the taxpayer has a reasonable excuse for late payment. A penalty charge notice will be issued against which the taxpayer will appeal within 30 days. The appeal will include his excuse for late payment. HMRC will review that appeal objectively before deciding whether the excuse is ‘reasonable’ in the context of the delay that has triggered the penalty.

HMRC's view of “reasonable excuse” is that it should involve an “unforeseeable and exceptional event” beyond the taxpayer's control. If HMRC does not uphold the appeal, the taxpayer has a right to appeal to the Tribunal. The Tax Tribunal normally has a slightly wider interpretation and generally takes criteria such as postal delays, adviser errors and illness into account.

For taxpayers with no reasonable excuse, the new late payment penalties will consist of 2 penalty charges:

- The first charge (an initial late-payment penalty) which is based upon payments and TTP agreements made in the first 30 days after the payment due date; and
- A second charge (a ‘penalty interest’ charge) which is based upon how long the debt remains outstanding after the initial 30 days.

Taxpayers who pay their tax late can still avoid a penalty if they either:

- Pay in full before the end of the 15-day period starting the day after the due date. This means that for tax payable on (say) 31 January, a penalty is avoided if full payment is made by midnight on 15 February; or

- Organise a Time To Pay (TTP) arrangement. 'Organise' means that the taxpayer should have submitted a TTP proposal to HMRC within the 15 days (rather than it being actually accepted in this period).

If a payment is made or a TTP is organised outside the 15-day period, a late payment penalty will be charged. The penalty is the "applicable percentage" of the outstanding tax. The penalty will be halved if either full payment is made within 30 days of the due date (i.e., between days 16 and 30) or if a TTP is organised in this 16-to-30 day period.

The "applicable percentage" will be set by statute in due course but suggestions are that this, like its predecessor, will be 5%.

If the tax remains outstanding 30 days after the day following the due date (i.e., on day 31), a second charge will kick-in. This will be an additional penalty, calculated in a similar way to interest, accruing from day 31.

In addition to the first and second penalty charges outlined above, interest at the prevailing HMRC rate will continue to be charged on any late paid tax. This will apply to all late payments (even those made within 15 days of the due date).

All this can be summarised in the Table below:

Number of days the payment is made late	Initial late-payment penalty	Penalty interest charge	'Standard' interest charge
1 - 15	No	No	Yes
16 - 30	Yes (50% reduction) penalty	No	Yes
31 and above	Yes	Yes	Yes

Penalty notices will be issued to taxpayers in respect of both the first and second penalty charges. Amounts shown as payable on the notice will be required to be paid, or appealed, within 30 days of the date of that notice.

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