Powers reviewed, powers extended

A large number of proposals in the Budget, *Francesca Lagerberg* says, will impact significantly on tax practitioners' lives

Budget 2008 has confirmed that the government is pushing ahead with a review of all existing powers relating to tax. This covers such issues as enquiries, penalties for incorrect returns and all forms of checking tax returns. The review has been ongoing ever since the Inland Revenue merged with Customs & Excise to form HMRC.

The first major piece of legislation in this review was in last year's *Finance Act*, with a new regime for penalties on incorrect tax returns for the main taxes. This takes effect from April 2008 for returns filed after April 2009, so we may already be beginning, or shortly starting on, work for returns that will be under the new rules.

The Budget included proposals to extend this legislation to all other taxes, and suggested a number of controversial ideas in relation to visits to business premises and compliance checks. The details are in Budget Notes 95 to 100, which can be found on www.hmrc.gov.uk.

Consultation process

All the proposals in the Budget have been subject to some consultation. Some issues were first looked at as far back as May 2007, but others were only fleshed out in January 2008, when the consultation period ran to 6 March. The problem was that the Budget was on 12 March 2008, leading to the perception that action was announced only six days after the consultation was closed. Can the responses really have been reviewed in full, and considered? The reality is that HMRC had been taking a lot of soundings on this issue, and many meetings between interested parties had taken place. We will see a response document shortly, setting out how HMRC considered those consultation replies; but it doesn't improve people's view of consultation when such short time-frames are involved.

The Budget itself included a large number of important proposals that will affect tax practitioners' day-to-day lives if they are enacted in their current form. Obviously these proposals are still subject to Parliamentary scrutiny, once they are published in the Finance Bill 2008, and some items may be amended before that Bill receives Royal Assent.

Incorrect returns

Schedule 24 to the *Finance Act* 2007 introduced a new framework for assessing penalties on incorrect returns, covering taxes such as income and corporation tax and VAT. This new regime takes effect for returns filed after April 2009, and penalties based on taxpayer behaviour will be imposed. The key to reducing penalties for errors will depend on whether the taxpayer took 'reasonable care', and the extent of disclosure they made (eg, was it unprompted or prompted?).

Budget 2008 extends this framework to almost all other taxes bar tax credits, which carry on in their current fashion. The Finance Bill 2008 will include provisions to bring in the *Finance Act* 2007-style regime for penalties for inheritance tax, environmental taxes, stamp duties and excise duties. This will affect returns filed on or after April 2010. This will not be without its problems, due to the difficulty of shoehorning in a 'one size fits all' approach to some of these taxes.

The way the penalty will be imposed is a simple extension to the rules set out in *FA* 2007, Sch 24. There will be no penalty where a taxpayer makes a mistake, but there will be a penalty of up to:

- 30% for failure to take reasonable care;
- 70% for a deliberate understatement; and
- 100% for a deliberate understatement with concealment.

For an unprompted disclosure of a failure to take reasonable care, the penalty could be reduced to nil. Where a taxpayer discloses fully when prompted by a challenge from HMRC, each penalty could be reduced by up to a half.

A new 'third party penalty' is introduced, although it has been modified from original proposals to seek to make it apply in limited circumstances. Where a return is incorrect because a third party (which could be a tax adviser) has deliberately provided false information or deliberately withheld information from the taxpayer with the intention of causing an understatement of tax due, a penalty could be charged on the third party.

In addition, *FA* 2007, Sch 24 will be extended to cover penalties for failing to register, or notify HMRC about, a new taxable activity. This will apply across all the taxes, levies and duties that HMRC administers, and will include late VAT registration. This element will take effect from 1 April 2009.

There still remains an obligation to notify in relation to Class 2 NICs for those who begin self-employment. However, the good news is that the existing fixed penalty of £100 for failing to notify within three months will be removed. It will however be replaced with a behaviour-based penalty.

Compliance checks

The new terminology to describe HMRC's checking that businesses and individuals are paying the famous 'right amount of tax' is 'compliance checks'. For income tax, corporation tax, capital gains tax, VAT and PAYE, new rules will apply from 1 April 2009.

These will include more stringent record-keeping requirements and a power to look at those records at business premises in 'real time'. This is highly controversial, and the main issue is how it will be implemented. Many businesses may not have perfect processes, but still produce enough in the way of records to prepare proper and correct returns. Different businesses also have different record requirements. For example, a simple business may have very little in the way of formal records. Although it is not clear from the Budget Notes, HMRC's thinking appears to be that, provided the business has adequate records to meet its obligations (eg, something as basic as all relevant papers in a shoebox), HMRC will not expect to see this available in some prescribed format – but it would want to see that records are being kept.

There will need to be a detailed training exercise, and probably a cultural shift on HMRC's part to ensure that these powers work as intended, and are not used as fishing expeditions or are undertaken without an understanding of how different types of business are run.

It is helpful though that the proposals confirm that visits will only be to business premises and not taxpayers' private residences, unless they use their home for business. Such visits will normally be announced in advance.

Assessment time limits will also be standardised, as follows:

Tax	Mistake	Discovery	Failure to take reasonable care	Deliberate understatement
VAT	4 years	N/A	4 years	20 years
IT & CGT	N/A	4 years	6 years	20 years
CT	N/A	4 years	6 years	20 years
PAYE	4 years	N/A	6 years	20 years

Time limits for taxpayers' claims will also be aligned, at four years.

Tax debt

Changes are also being made to the way HMRC manages tax debt. For example, by the autumn of 2008 it will be accepting payment by credit card. Other changes include giving HMRC the ability to offset repayments against tax liabilities, and greater debt-enforcement powers.

HMRC will be able to set the repayments it must make to individuals and businesses against the payments those individuals and businesses owe.

Tribunal reform

The Ministry of Justice is overseeing major changes to the way tribunals operate in the UK. The *Tribunals, Courts and Enforcement Act* 2007 brought in the idea of a new first-tier tribunal, which will see the end of the general and special commissioners as we know them, from 2009. The Budget confirmed that the Finance Bill 2008 will include a power to introduce secondary legislation to change the way appeals against HMRC are handled in the light of those changes. It is probable that this will include the introduction of a statutory internal appeals procedure.

Concessions after *Wilkinson*

A few years ago, the House of Lords decision in *Wilkinson* [2005] BTC 281 raised concerns about whether HMRC was able to make extra-statutory concessions. The upshot has been that there have been no significant concessions since that case and a fear from HMRC of changing existing ones. The Budget confirmed that, after taking legal advice, HMRC believes that its existing concessions are within its 'collection and management' discretion and therefore should survive. It is intending to legislate a significant proportion of them by Treasury Order, and will do this via a power introduced in the Finance Bill 2008.

Taxpayers' Charter

We will also be seeing the beginning of a discussion process leading to the introduction of a new Taxpayers' Charter. Such a document existed in the 1980s and then gradually fell into disuse before being removed. The intention is for it to set out taxpayer rights and obligations. A Charter will bring the UK into line with most other developed countries, and is a welcome development.

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