CHAPTER 11

AN INTRODUCTION TO SELF ASSESSMENT

In this chapter you will learn about the self assessment regime covering the following topics:
- the filing of tax returns;
- notifying chargeability;
- deadlines, interest and penalties;
- amendments and enquiries.

11.1 Introduction

The UK tax system is administered generally by Central Government, but the Ministry concerned with the collection and imposition of taxes, is the Department of the Treasury. The Treasury is also known as the Exchequer, and at the head of this Department you will find the Chancellor of the Exchequer.

The administration of taxes in the UK is in the hands of The Commissioners for Her Majesty's Revenue and Customs (HMRC). As the name suggests, the Commissioners are technically appointed by the Crown. The Commissioners in turn appoint civil servants to do the actual work of administration. These civil servants are called Officers of Revenue and Customs.

In this chapter and the ones that follow it, we are concerned with the administration of income tax and capital gains tax. Rather than use the long-winded name of HM Revenue and Customs, we will refer simply to them as “HMRC”.

HMRC manage the UK tax system on a day to day basis through a Local Compliance Structure organised on a functional basis. This is divided into three taxpayer or “customer” groups, being Large and Complex Businesses (LCB); Small and Medium Sized Enterprises (SME) and Individuals and Public Bodies (IPB). Customers in the LCB and SME groups have all tax matters dealt with by the same business unit. The Local Compliance teams also carry out enquiries. The Specialist Investigations office deals with complex and serious cases which are not suitable to be dealt with by Local Compliance, due to their size, nature, complexity or seriousness.

A two-tier tribunal system – the First-tier Tribunal and the Upper Tribunal – deals with points of dispute between taxpayers and HMRC.

Self Assessment is the regime by which HMRC assesses and collects direct tax in the UK.

11.2 Tax Returns

In the UK at present, around 30 million people pay tax. Out of those 30 million people, over 12 million prepare income tax returns under the Self Assessment system.

Taxpayers who are self-employed must submit tax returns, as may individuals whose taxable income is above the basic rate limit and who therefore, pay tax at
the higher and/or additional rate. Taxpayers who have **untaxed** income (i.e. rents, National Savings interest etc) also have to file tax returns.

Finally, any taxpayer who has made a chargeable **capital gain** in the year, also has a duty to submit a tax return.

There are around 18 million people in the UK who pay income tax but do **not** have to fill in an income tax return. These will primarily be **employees** whose tax is deducted at source under the Pay as you Earn system (PAYE). Similarly **basic rate** taxpayers, who do not owe any more tax on their interest or their dividend income, do not normally need to fill in a tax return.

### 11.3 Notification

If an individual becomes **chargeable** to income tax or capital gains tax for the **first time**, he has a duty to **notify** HMRC within **6 months** of the end of the tax year in which he became chargeable. **TMA 1970, s.7(1)**

For example an individual who starts to receive rental income in the tax year 2015/16, has until 5 October 2016 to notify HMRC.

If the taxpayer misses this deadline, HMRC will charge a **penalty**. **FA 2008, Sch 41**

The penalty will be based on the behaviour of the person concerned and is a **percentage of the ‘potential lost revenue’**. The potential lost revenue to which any penalty will apply is the **amount of the income tax (including Class 4 National Insurance Contributions) and/or capital gains tax unpaid at 31 January following the tax year**, as a result of the failure to notify. **FA 2008, Sch 41 para 7(2)**

For a **deliberate and concealed failure**, the penalty will be a **maximum 100%** of the potential lost revenue; for a **deliberate but not concealed failure**, the **maximum penalty will be 70%** of the potential lost revenue; and for any other case – e.g. due to lack of care, the **maximum penalty will be 30%** of the potential lost revenue. **FA 2008, Sch 41 para 6(2)**

A failure is deliberate and concealed where the failure is deliberate and the taxpayer **makes arrangements to conceal the situation** giving rise to the obligation. This would include creating false evidence of a non-taxable source of income to explain undisclosed income; creating false invoices to support inaccurate turnover figures or destroying books and records. **FA 2008, Sch 41 para 5**

A failure is deliberate but not concealed where the failure is deliberate but no arrangements are made to conceal the situation giving rise to the obligation. An example of this would be where a person is aware of the obligation to notify a source of income but decides not to do so, without taking steps to conceal the income.

**Reductions in the amount of the penalty are available for both ‘unprompted’ and ‘prompted’ disclosures.**
The table below details the maximum and minimum penalties that could apply. Note that where the taxpayer is simply careless in not making the necessary notification, the reduction in the penalty also depends on how long has elapsed since any tax (or NIC) first became unpaid as a result of the failure. FA 2008, Sch 41 para 13

<table>
<thead>
<tr>
<th>Behaviour</th>
<th>Maximum penalty</th>
<th>Min penalty with unprompted disclosure</th>
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Disclosure is unprompted if the taxpayer has no reason to believe HMRC have discovered or are about to discover the failure.

Disclosure takes place where a taxpayer tells HMRC about the failure, gives HMRC reasonable help in calculating the resulting unpaid tax and allows HMRC access to records to check the amount of unpaid tax. FA 2008, Sch 41 para 12

The actual reduction in the penalty depends on the quality of the elements of disclosure, including timing, nature and extent.

Increased percentages apply where the late notification relates to an offshore matter, such as income arising or assets held overseas. The actual rates depend on whether the overseas country is a category 1 territory, for example Canada, in which case the above rates apply, or a category 2 or 3 territory in which case increased rates apply as set out in the legislation. For example, Greenland is a category 2 territory and Brazil is a category 3 territory. For exam purposes you are not required to know which countries make up which categories.

A self-employed individual must also notify HMRC that they are liable for Class 2 National Insurance Contributions (NICs). Notification must be made as soon as possible – in practice a self-employed individual will notify HMRC for both tax and Class 2 NICs by registering his business with them.

If notification for Class 2 NIC does not take place by 31 January following the end of the tax year in which the liability first arose, a penalty will be charged. This is identical to the late notification penalty for income tax purposes, with the relevant percentage applied to “lost contributions”. Lost contributions are the contributions due between the date the individual first became liable to pay a Class 2 contribution and 31 January before HMRC received notification of liability. SI 2001/1004 Reg 87B

Illustration 1

Oscar started to trade as a self-employed individual on 1 July 2015. He was very successful and as a result did not have time to consider his self assessment responsibilities. As a result he did not notify HMRC of his self employment by 5 October 2016. HMRC contacted Oscar in July 2017 and as a result Oscar appointed a tax adviser. HMRC were notified of the self employment. The tax return for 2015/16 was filed in August 2017 showing tax and Class 4 NIC due of £15,000.
Explain the penalties due for late notification.

It would appear that the failure to notify HMRC of the self employment by 5 October 2016 was due to carelessness, as Oscar did not deliberately decide not to notify HMRC.

The maximum penalty is therefore 30% of the potential lost revenue of £15,000, which is the liability which should have been paid by 31 January 2017. However, Oscar made a prompted disclosure within 12 months of the tax becoming unpaid, so the penalty may be reduced to a minimum of 10% of the potential lost revenue.

In addition, he will also be charged an additional penalty as he failed to notify his liability for Class 2 NIC. A penalty of between 10% and 30% of the Class 2 NIC due between 1 July 2015 and 31 January 2017 will be charged.

Failure to notify penalties must be paid within 30 days of the date the notice assessing the penalty is issued, or interest will be charged. FA 2008, Sch 41 para 16

The decision to issue a penalty or the amount of the penalty can be appealed against. FA 2008, Sch 41 para 17 & 18

Penalties will not be charged if the taxpayer has a reasonable excuse for the failure and the failure is not deliberate. FA 2008, Sch 41 para 20

The “notification of chargeability” provisions only apply to taxpayers who have not already received a tax return from HMRC. If a taxpayer receives a tax return, any income received or gains made in the tax year can simply be disclosed on the tax return in the normal way.

11.4 Issue of a Tax Return

Tax returns are typically issued by HMRC to taxpayers on 6 April immediately following the tax year. Therefore, tax returns for the year ended 5 April 2016 - i.e. returns for the 2015/16 tax year - will usually be issued the day after the end of the year - ie on 6 April 2016. If the taxpayer filed an online return for the previous year they will be sent a notice to fill in a tax return.

Every tax return requires the taxpayer to provide certain details. All taxpayers must give details of all income received from all sources in the tax year.

Certain allowances to be claimed by the taxpayer also need to be claimed within the tax return. For instance, a taxpayer born before 6 April 1935 entitled to the married couple’s allowance needs to claim that allowance on the return.

Any other claims for relief also have to be made on the tax return. For example, any deductible payments, any tax reducers, any contributions to pension schemes etc, which qualify for tax relief, must be claimed within the tax return. TMA 1970, s.42

As well as sending the taxpayer a basic tax return, HMRC add on supplementary pages to the end of the basic form depending on the particular source of income. For example, employees will receive employment pages, those with rental properties receive property income pages, and so on.

Individuals with many different sources of income therefore have to complete a number of separate supplementary pages, as well as the basic tax return.
Once the taxpayer has completed the tax return, he will sign a declaration to say that to the “best of his knowledge and belief” the tax return is “correct and complete”.

If the tax return turns out not to be correct and complete - i.e. there are errors or omissions - HMRC have powers to charge penalties for incorrect returns. FA 2007, Sch 24

11.5 Filing Deadlines

There are two separate dates for filing a return, depending on whether the taxpayer is filing a paper return or an electronic / online return.

Where the taxpayer completes a paper return, the return should normally be filed no later than 31 October following the end of the tax year. TMA 1970, s.8(1D)(a)

Therefore for the tax year 2015/16, the paper return must normally be filed by 31 October 2016. However, the paper return can be filed within three months of the date of issue of the return if this is later than the following 31 October. TMA 1970, s.8(1F)(a)

Where a taxpayer completes an online return, the return should normally be filed no later than 31 January following the tax year. TMA 1970, s.8(1D)(b)

Therefore for 2015/16, the online return must normally be filed by 31 January 2017. However, the online return can be filed within three months of the date of issue of the return or notice if this is later than the following 31 January. TMA 1970, s.8(1G)

Illustration 2

Assume that a 2015/16 tax return is issued by HMRC to a taxpayer on 25 November 2016.

State the deadline for filing the return.

As the return has been issued after 31 October the deadline for filing the return (whether a paper return or online) is 3 months from issue of the return, being 25 February 2017.

If the return is filed by 25 February 2017, HMRC cannot charge any late return penalties.

Where a taxpayer has tax deducted at source via the PAYE system, underpayments of tax of less than £3,000 can be collected via PAYE rather than a one-off payment. In order for this treatment to apply, if the taxpayer is filing an online return, the tax return must be filed by the earlier deadline of 30 December following the end of the tax year. SI 2003/2682 Reg 186

11.6 Calculation of Tax

If a taxpayer files a return online, he does not have to worry about calculating his own tax liability. HMRC software will automatically calculate the tax liability.

If the taxpayer is filing a paper return, he can “self assess” his tax liability using the “Tax Calculation Summary”. However, where a return is submitted by 31 October (or 2 months from the issue of the tax return if later) HMRC will calculate the tax for the taxpayer if he wishes. TMA 1970, s.9(2)
This means that the taxpayer will tell HMRC what his income and allowances are and HMRC will calculate the tax on his behalf. The taxpayer can of course still calculate his own liability if he wishes to. If the taxpayer does not want to calculate his own tax for the year, HMRC will simply work out the tax he owes from the income and allowances included within the tax return. They will then send a statement to the taxpayer, telling him how much tax he owes or how much is repayable.

**Illustration 3**

Assume HMRC send a taxpayer his 2015/16 tax return on 3 September 2016.

**Explain the deadlines for filing a paper return.**

If the taxpayer wishes to file a paper return, but does not want to self-assess, then he must submit the return by the later of:

a. 31 October 2016, or

b. 2 months from issue of the return, being 3 November 2016.

As long as this return is filed by 3 November 2016, HMRC will calculate the tax liability for the taxpayer.

If the taxpayer wishes to file a paper return and is happy to self-assess the deadline is the later of:

a. 31 October 2016, or

b. 3 months from the date of issue of the return, being 3 December 2016.

You can see that where a return is issued late, the deadline for filing a paper return differs depending on whether the taxpayer wishes to self assess or not.

If the taxpayer misses the 3 December 2016 deadline, he can avoid a penalty by making sure his return is submitted by 31 January 2017. However, in this case the taxpayer would have to file the return online in which case his tax liability will be calculated automatically.

**11.7 Short Tax Returns**

Taxpayers who have relatively simple tax affairs may receive a four page Short Tax Return instead of the longer return. Examples of the type of taxpayer who may be issued with a Short Return include employees (who are not directors) with taxable benefits, self employed traders with turnover of less than £82,000 (2015/16), people in receipt of UK property income below £82,000 and pensioners who have pensions and straightforward investment income.

Examples of people who cannot use the short tax return form include those in partnership, people who received income from a trust and those who received income from abroad in excess of taxed foreign dividends of £300.

The form is short and simple and has no facility to self assess. A simple guide is included for taxpayers who want to make a rough calculation of the tax due.
11.8 Penalties for late returns

Schedule 55 FA 2009 contains penalty provisions in respect of failure to make a return.

An initial penalty of £100 will apply if a return is late, even where there are no amounts outstanding. Additional daily penalties of £10 per day may be levied in respect of returns which are more than 3 months late. The daily penalty can be imposed for a maximum of 90 days. FA 2009, Sch 55 paras 3 & 4

If a return is more than 6 months late, there will be an additional penalty of 5% of any liability to tax which would have been shown in the return or £300 if greater. The liability to tax is the tax due for the year, after tax deducted at source. It is not reduced by any amount paid towards that liability. FA 2009, Sch 55 para 5

An additional penalty of 5% of any liability to tax (or £300 if greater) will also be levied if the return is more than 12 months late. If the return has not been submitted within 12 months and by failing to make the return the taxpayer is deliberately withholding, but not concealing information, which would enable HMRC to assess the tax liability, the maximum amount of the penalty increases to 70% (or £300 if greater). If the withholding of information is deliberate and concealed, the maximum amount of the penalty is 100% of the tax liability (or £300 if greater). FA 2009, Sch 55 para 6

Illustration 4

Harris received notice to file an income tax return for 2015/16 on 6 April 2016. He intended to file the return on-line but did not actually file the return until 1 March 2017.

Calculate any late filing penalty due for Harris.

As Harris did not file the return by the due date of 31 January 2017, he will be liable to a fixed £100 penalty.

Illustration 5

Mardy filed his 2015/16 income tax return online on 1 August 2017. He had received a notice to file the return on 6 April 2016. The return showed a liability to tax of £12,000.

Calculate any late filing penalties due for Mardy.

As the return was not filed by 31 January 2017 a fixed £100 penalty will be levied.

HMRC could decide to impose daily penalties of £10 per day for a maximum of 90 days as the return was outstanding for more than 3 months.

Finally, as the return was outstanding for more than 6 months, a penalty of £12,000 × 5% = £600 will be charged.

Penalties that apply where a person has deliberately withheld information, can be reduced for both prompted and unprompted disclosure of the information. FA 2009, Sch 55 para 14

Disclosure takes place where a taxpayer tells HMRC about the relevant information, gives HMRC reasonable help in quantifying the tax unpaid as a result
of the information being withheld and allows HMRC access to records to check the amount of unpaid tax.

Disclosure is unprompted if it is made when there is no reason to believe that HMRC have discovered or are about to discover the information.

The actual reduction in the penalty depends on the quality of the disclosure, including timing, nature and extent.

The table below details the maximum and minimum penalties that could apply:

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The minimum penalty is £300 if greater.

HMRC have the power to reduce the penalty if there are special circumstances.

The maximum aggregate penalty (calculated as a percentage of the liability to tax) that can be charged in respect of the late filing of a return is 100% of the liability to tax. [FA 2009, Sch 55 para 17(3)]

As with late notification penalties, increased percentages apply where the deliberate withholding of information relates to income arising or assets held overseas where the overseas country is a category 2 or category 3 territory.

Where a penalty for a late return is calculated based on a tax liability, the amount of the penalty is reduced by any other penalty calculated in relation to the same liability, for example a failure to notify penalty. However, the penalty is not reduced by a penalty for late payment of tax. In other words, if a return is filed late and the tax liability is paid late, the taxpayer will incur both late filing and late payment penalties.

Late payment penalties must be paid within 30 days of the date the notice of assessing the penalty is issued, or interest will be charged. [FA 2009, Sch 55 para 18]

The decision to issue a penalty or the amount of the penalty payable can be appealed against by the taxpayer. [FA 2009, Sch 55 para 20]

Penalties will not be charged if the taxpayer has a reasonable excuse for the failure. [FA 2009, Sch 55 para 23]

### 11.9 Amendments

HMRC have the right to amend the taxpayer's return within nine months of the date of receipt. HMRC will usually do this to eliminate or to reverse any obvious errors or mistakes within the return. These are usually arithmetical errors although the HMRC can reverse any technical mistakes made by the taxpayer in completing the return. HMRC will notify the taxpayer of any amendments made. [TMA 1970, s.9ZB(3)]
The taxpayer also has the right to amend the return already submitted, so long as this is within twelve months of the due date for filing. For example, if a taxpayer realises he has made an error in the return after having filed it, he can write to HMRC to reverse the error or mistake. The due date for filing, for amendment purposes, is 31 January following the tax year (or 3 months after the return was issued if later). TMA 1970, s.9ZA (2) & (3)

11.10 Recovery of Overpaid Tax

Where the 12 month deadline for a taxpayer to amend a return has passed, a claim can be made in certain circumstances to recover tax overpaid as a result of a mistake. The claim must be made within 4 years of the end of the relevant tax year, so if a taxpayer has made a mistake in the tax return for 2015/16 a claim for relief must be made by 5 April 2020. TMA 1970, Sch 1AB

For example, if a sole trader claimed advertising expenses of £150 when the actual expenses incurred were £1,500, then a claim for relief can be made.

However, if there is any other means of obtaining the relief for example by making or amending a self-assessment return, this method must be used in priority to overpayment relief.

If the matter has already been the subject of an appeal to the Tribunal then no claim can be made.

A claim cannot be made where the tax return was prepared in accordance with the practice generally prevailing at the time, unless the tax was charged contrary to EU law.

A claim cannot be made where the mistake is in a claim or election. In addition, a claim cannot be made if the mistake consists of the actual making of a claim or a failing to make a claim. For example, if a taxpayer made a claim to set a trading loss against income of a year in which they were a basic rate taxpayer, rather than in a year in which they were a higher rate taxpayer, overpayment relief cannot be claimed. Additionally, if a taxpayer could have claimed relief for a trading loss against other income but the claim was not made, again no relief will be available under these provisions.

Instead, if a mistake has been made in a claim, an amendment can be made within 12 months from the normal filing date of the return or date on which the claim was made. If this 12 month deadline has passed, provided the time limit for making the original claim has not expired, a supplementary claim can be made. TMA 1970, s.42(9)

If a claim has not been made within the time limit, HMRC do have the means to accept late claims, in limited cases, for example if there has been a relevant error by HMRC.

11.11 Enquiries

HMRC have the right to make a formal “enquiry” into every tax return submitted to them. This enables them to look closely at the individual entries within the return and very often, taxpayers will be asked to support each entry with the relevant documentary evidence. TMA 1970, s.9A

Most enquiries are risk-based selections, although each year HMRC will also select a random number of taxpayers for an enquiry. This is intended to be a deterrent –
ie, an incentive for taxpayers to get their tax returns right just in case they are selected for a random enquiry. HMRC have two categories of enquiry. Full enquiries cover the return as a whole and aspect enquiries deal with an individual item or a group of items on a tax return. For example, HMRC may ask the taxpayer for documentary evidence to support a particular claim for tax relief, or they may ask, for example, for dividend vouchers to verify that the figure on the tax return in respect of dividend income is correct.

Bear in mind that HMRC receives information from certain third parties about income received by taxpayers. For example, UK banks and building societies will give details to HMRC of any interest paid to UK taxpayers. Therefore, HMRC wants to make sure that the individual's tax return is consistent with the information they already have.

The most common target for risk—based enquiries are the self-employed who are regularly asked to produce their books and records to support the details on the tax return. In particular, cash trades such as pubs, market traders, taxi drivers etc., are a favourite source of HMRC enquiries.

To commence an enquiry, a Revenue Officer must issue a formal “Enquiry Notice” to the taxpayer under s.9A TMA 1970 within the “time allowed”. The normal time limit for commencing an enquiry is twelve months after the day on which the return is delivered. TMA 1970, s.9A (1) & (2)(a)

This means that for a 2015/16 tax return, if HMRC wishes to commence an enquiry into that return, and it was delivered on, say, 15 December 2016, the taxpayer must receive the notice no later than 15 December 2017.

If the return is submitted late - ie. the taxpayer misses the 31 January filing deadline - the deadline for HMRC to raise a formal enquiry into the return is extended. The final date for raising an enquiry is extended to the end of the calendar quarter following the anniversary of the actual filing date of the return. Here calendar quarters end on 30 April, 31 July, 31 October and 31 January. TMA 1970, s.9A(2)(b)

A taxpayer is permitted to make amendments to the return while the enquiry is in progress although HMRC will not process such amendments until the enquiry is completed. TMA 1970, s.9B

During the enquiry the parties may jointly refer questions to the Tribunal for their consideration and determination. TMA 1970, s.28ZA

Once the enquiry has been completed, HMRC will issue a “closure notice”. This will include a statement of HMRC’s conclusions and any amendments to the return deemed necessary as a result of the enquiry. The taxpayer has 30 days to appeal against any amendments included with the closure notice. TMA 1970, s.28A; TMA 1970, s.31(1)(b)

HMRC may only enquire into a tax return once. Therefore, once a closure notice has been issued, HMRC may not raise further enquiries into the return (for instance, if they felt their enquiries were inadequate or not sufficiently wide-reaching). This is subject to the rules on “discovery”. TMA 1970, s.9A(3)

An enquiry may be opened into an amendment to the tax return (this is effectively treated as a separate return for enquiry purposes). However the enquiry will be restricted to matters covered in the amendment, and cannot extend to the original return. TMA 1970, s.9A(5)
11.12 Estimates and Provisional Figures

If a taxpayer does not have final figures prior to the filing date for a return, he should enter provisional figures on the return rather than miss the filing deadline. The provisional figures should clearly be identified in the tax return. Once the correct figure is available, it should be notified to HMRC together with any amended self assessment. A penalty could be charged if the taxpayer did not have a good reason for supplying provisional figures or provided unreasonable ones.

Estimated figures may be included on a tax return. The taxpayer may wish the figures to be accepted as final, for example where an accurate figure cannot be provided because records have been lost. Such figures must be identified on the tax return.

However, if the taxpayer considers the estimates to be reliable, for example the private proportion of a business expense, there is no need to draw attention to the figures.

11.13 Record Keeping

It is easier to keep one’s returns up to date and avoid interest and penalties etc., if we retain full and proper records. TMA 1970, s.12B

Taxpayers are required to retain records of income and capital gains for at least 22 months after the end of the tax year to which they relate i.e. the first anniversary of 31 January following the end of the tax year.

Taxpayers who are self-employed or who have income from property must retain records for at least five years and ten months after the end of the tax year to which they relate i.e. the fifth anniversary of 31 January following the end of the tax year.

In certain situations, records must be kept for longer than the minimum periods stipulated above i.e.

1. if there is an enquiry into the return which has not been completed by the date for which records must normally be retained. In this event, records must be kept until the enquiry is completed;

2. if the return is submitted late, the period within which HMRC can commence an enquiry is extended. In this instance records must be kept until the final date for commencing an enquiry has passed.

Penalties may be charged for failure to retain proper records. The maximum penalty is £3,000 for each failure to maintain records sufficient to support entries on the return. The Revenue will consider each case on its merits and have power to mitigate this penalty. Appeals against the imposition of such penalties may be made to the Tribunal. TMA 1970, s.12B(5)

11.14 Determinations

Where a tax return is not filed by the filing date HMRC may make an estimate of the tax due to the best of their information and belief. This is known as a determination and is treated as a self assessment. The taxpayer cannot appeal against a determination but it is automatically replaced once the actual self
assessment is filed. The tax charged by a determination is payable on the normal
due date for the liability for the year.  **TMA 1970, s.28C**

A determination cannot be made after three years from the due date for the
return. A determination can only be replaced by an actual self assessment made
within the same period, or 12 months from the date of the determination if later.

However, if a determination has been made and the taxpayer has paid or been
assessed for tax that is not due, he may be able to claim relief under Schedule 1AB
(Recovery of Overpaid Tax) even if a self-assessment has not been made in time.
Although relief is not usually available under this Schedule more than 4 years after
the end of the relevant tax year, a 'special relief' will apply where a determination
has been made if certain conditions are met. The conditions are that:

- HMRC believe it would be unconscionable to seek to recover the full amount
due (or withhold repayment of it if it has already been paid); and
- the taxpayer's tax affairs are up to date or satisfactory arrangements have
been put in place to bring them up to date; and
- either this is the first time the taxpayer has used the special relief or there are
exceptional circumstances such that they should be allowed to do so again.
  **TMA 1970, Sch 1AB, para 3A**

**11.15 Appeals**

If a taxpayer disagrees with a decision made by HMRC in relation to a direct tax
such as income tax, he can challenge the decision by appealing. A taxpayer may
bring about an appeal for a number of reasons:  **TMA 1970, s.31**

- The legislation is unclear or open to different interpretation;
- The taxpayer takes a different view to HMRC on the interpretation of the
  legislation, or the taxpayer does not accept HMRC's published view in a Press
  Release or Statement of Practice, etc;
- The taxpayer believes HMRC has made a mistake which has not been
  rectified (for example, an incorrect amendment to a return or any incorrect
  conclusion to a closure notice after an enquiry).

A taxpayer will have a right to appeal an amendment or HMRC assessment if the
taxpayer has reason to believe the calculation of tax liability is incorrect.

Notices of appeal must be given in writing within 30 days of the amendment or
assessment etc as appropriate. The notice should give the grounds for the
appeal.  **TMA 1970, s.31A**

Appeals sent to HMRC after the 30 day appeal period has passed may be
accepted if there is a reasonable excuse for why the appeal is late. If HMRC do
not accept the late appeal, an appeal can be made to the Tribunal (see later) to
accept the late appeal.  **TMA 1970, s.49**

At the same time as making the appeal, the taxpayer may apply for
postponement of any tax (or additional tax) which HMRC believe is due. However,
if any of the postponed tax is subsequently found to be due, interest will be
charged on any unpaid amount. If no postponement application is made, the tax
must be paid (and perhaps later repaid if the appeal is successful).
Appeals are made in the first instance to HMRC. Most appeals are determined by agreement between HMRC and the taxpayer without the need to involve the Tribunal.

For example, HMRC may make an amendment to a self-assessment, which is incorrect. The taxpayer will appeal HMRC's revised self-assessment stating the reasons for the appeal. The Officer will consider the appeal by reviewing the amendment and determine the appeal by agreement. TMA 1970, s.54

If an appeal cannot be settled by agreement HMRC may offer a review, in which case the taxpayer must accept the offer in writing within 30 days of the offer being made. If the taxpayer does not wish to accept the review offer, they must appeal to the Tribunal within the same 30 day period. TMA 1970, s.49A-s.49E

If a review is not offered, the taxpayer can either ask HMRC to review their decision or ask the Tribunal to consider the appeal.

A review involves HMRC appointing an officer, not previously involved with the case to carry out a review of the decision. The taxpayer can put their case to the officer, usually in writing. A review is generally carried out within 45 days. If it takes longer, HMRC should obtain the taxpayer's agreement to the longer period. If the taxpayer is not notified of the outcome within the review period an appeal can be sent to the Tribunal.

When the review is completed the review officer will state their decision on the matter. If the taxpayer does not agree with the decision of the review officer he can ask for the appeal to be heard by the Tribunal, within 30 days of the date of the review conclusion letter.

The Tribunal is an independent legal body which consists of independently appointed expert tax Judges and/or panel members.

There are two tiers of the Tribunal, the First-tier Tribunal and the Upper Tribunal. At the First-tier, tax appeals are heard within the Tax Chamber. The Upper Tribunal is a Superior Court of Record with all the powers and authority of the High Court. There are four Chambers in the Upper Tribunal, one of which is the Tax and Chancery Chamber, where tax appeals are heard. TCEA 2007, s.3

Almost all tax appeals will start in the First-tier Tribunal. It is possible in rare cases for complex cases to go directly to the Upper Tribunal, however the Tribunal will decide which cases should start in the Upper Tribunal.

Once the appeal has been received, the First-tier Tribunal will decide which of four categories it falls into – default paper, basic, standard or complex. SI 2009/273 para 23

If the case is determined as default paper, the Tribunal notify HMRC of the appeal. HMRC have 42 days to provide a statement of case, which is also sent to the taxpayer who has 30 days to respond if they wish. In most cases no hearing is required, although the taxpayer can request one. The tribunal will issue its decision in writing. Matters such as fixed filing penalties will be dealt with by default paper cases. SI 2009/273 paras 25 & 26

Basic appeals are dealt with at an informal hearing, where both the taxpayer and HMRC present their case. The decision is usually issued at the end of the hearing.

Standard and complex cases are dealt with at more formal hearings. In these cases, HMRC have 60 days to provide a statement of the case and the taxpayer
has 42 days to respond. The appeal will then be heard and a decision issued in writing within 28 days.

Appeals against a decision of the First-tier Tribunal are made to the Upper Tribunal. Permission must be obtained from the First-tier or Upper Tribunal before the appeal can be made – the request must be made in writing within 56 days of the date that the decision of the First-tier Tribunal was received. Appeals can only be made on a point of law. 

Decisions made by the Upper Tribunal are binding on both the taxpayer and HMRC unless either party appeals the decision to the Court of Appeal (again permission is needed from the Upper Tribunal or the Appeal Court) and finally (in exceptional cases) to the Supreme Court. A decision by the Supreme Court is final and conclusive and will establish a case law precedent that will stand (unless superseded by statutory changes) for reference in future cases. Once again, appeals can only be made on a point of law.

Appeals through the Court system are expensive and time-consuming and will (in the event of the case being lost) often result in costs being awarded against the unsuccessful party.

11.16 Penalties for Incorrect Returns - Introduction

Penalties will apply where a tax return or claim for a relief contains an inaccuracy which leads to an understatement of tax; or a false or inflated statement of a loss; or a false or inflated claim to a tax repayment. Penalties will be charged if the error occurred due to a careless action i.e. failure by the taxpayer to take reasonable care. This would apply, for example, if insufficient records were maintained or if a taxpayer estimated figures rather than obtaining accurate information.

In addition, greater penalties will be charged if the error is deliberate i.e. the person knowingly and intentionally submits an incorrect document but does not take steps to hide the error, for example deliberately including an incorrect turnover figure on a return but without creating false records to conceal the inaccuracy. Another example of a deliberate but not concealed error would be deliberately describing transactions inaccurately or in a way likely to mislead.

Finally an even greater penalty will be levied if the error is deliberate and concealed i.e. an incorrect document was sent knowingly and intentionally and active steps were taken to hide the error, such as creating false invoices or destroying books and records so that they are not available.

If a return contains more than one error, a penalty is charged for each error.

The penalty charged will be a percentage of the potential lost revenue.
The table below details the maximum and minimum penalties that could apply. 
FA 2007, Sch 24 para 4 and para 10

<table>
<thead>
<tr>
<th>Behaviour</th>
<th>Maximum penalty</th>
<th>Min penalty with unprompted disclosure</th>
<th>Min penalty with prompted disclosure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deliberate and concealed</td>
<td>100%</td>
<td>30%</td>
<td>50%</td>
</tr>
<tr>
<td>Deliberate but not concealed</td>
<td>70%</td>
<td>20%</td>
<td>35%</td>
</tr>
<tr>
<td>Careless</td>
<td>30%</td>
<td>0%</td>
<td>15%</td>
</tr>
</tbody>
</table>

As with late notification penalties and penalties for late filing, increased percentages apply where the inaccuracy relates to an offshore matter, such as income arising or assets held overseas, where the overseas country is a category 2 or category 3 territory.

Reductions are available for both ‘unprompted’ and ‘prompted’ disclosures.

Disclosure is unprompted if the taxpayer has no reason to believe HMRC have discovered or are about to discover the failure.

Disclosure takes place where a taxpayer tells HMRC about the failure, gives HMRC reasonable help in calculating the resulting unpaid tax and allows HMRC access to records to check the amount of unpaid tax. FA 2007, Sch 24 para 9

The actual reduction in the penalty depends on the quality of the elements of the disclosure, including timing, nature and extent.

Illustration 6

Peter has a portfolio of investment properties producing rental income. He is a higher rate taxpayer. He files his tax return for 2015/16 on 30 January 2017. The return shows his property income to be £72,000. Due to carelessness on Peter’s part, his property income should have been declared to be £90,000.

Calculate the maximum penalty that Peter could be charged by HMRC for his error.

The potential lost revenue as a result of Peter’s error is: 
(90,000 − 72,000) = 18,000 × 40% (income tax) £7,200

Peter’s error is careless so the maximum penalty for the error is: 
7,200 × 30% £2,160

This penalty will be charged in addition to the extra tax of £7,200 and in addition to any interest Peter will have to pay if the tax is paid after the normal due date for payment.

Note here that if Peter discovers the error before HMRC and he voluntarily discloses his mistake, the penalty can be reduced, potentially to NIL.

HMRC have the power to reduce the penalty if there are special circumstances.

You will see that these penalty provisions are very similar to the failure to notify penalties we have already looked at.
One difference to note is that there are no penalties for inaccuracies where the person has taken reasonable care. For example, an inaccuracy resulting from an arithmetical or transposition error which is not large in either absolute terms or in relation to the overall liability such that it would be identified in a review, would not result in a penalty. So, reporting a car benefit figure as £5,120 instead of £5,210 would not incur a penalty but reporting interest of £100 instead of £100,000 would!

However, an inaccuracy which was not careless or deliberate at the time the return was submitted will be treated as careless if the person discovers the inaccuracy at a later date but does not take reasonable steps to inform HMRC. FA 2007, Sch 24 para 3(2)

One other difference to the late notification penalty is that the reduction in a penalty for a careless error does not depend on when HMRC discover the inaccuracy.

Penalties can also be charged if an assessment issued by HMRC understates the liability and the taxpayer fails to take reasonable steps to notify HMRC within 30 days from the date of issue of the assessment. The rate of the penalty is the same as for a careless error. FA 2007, Sch 24 para 2

11.17 Penalties for Incorrect Returns – Potential Lost Revenue

The potential lost revenue is generally the extra tax due as a result of the discovery of the error. FA 2007, Sch 24 para 5(1)

Where an inaccuracy has the result that a loss is wrongly recorded and the loss has been wholly used, then the potential lost revenue is the amount of tax (and NIC) due or payable as a result of correcting the inaccuracy. FA 2007, Sch 24 para 7

In cases where the loss has not been wholly used, it is the sum of:

a. The potential lost revenue in respect of the amount of the loss used to reduce the tax due or payable; plus

b. 10% of any part that has not been so used.

If the calculation of the potential lost revenue in respect of more than one inaccuracy depends on the order in which they are corrected, a “careless inaccuracy” is taken to be corrected before a “deliberate inaccuracy”. Similarly a “deliberate, but not concealed” inaccuracy, is taken to be corrected before a “deliberate and concealed” inaccuracy. FA 2007, Sch 24 para 6

11.18 Penalties for Incorrect Returns - Other Points

If a penalty is charged due to failure to take reasonable care, it may be suspended for two years provided the suspension conditions agreed with HMRC are kept and no further penalties are incurred in the suspension period. If the conditions are met throughout the suspension period, the penalty will be cancelled. FA 2007, Sch 24 para 14

The ability to suspend a penalty is intended to support those who try to meet their obligations by giving them time to improve their systems, which help them to avoid penalties for inaccuracies in the future.

Suspension of a penalty is not possible where it relates to an error that was deliberate or deliberate and concealed.
A penalty in respect of an inaccuracy must be paid within 30 days of the date the notice assessing the penalty is issued, or interest will be charged. FA 2007, Sch 24 para 13

The decision to issue a penalty or the amount of the penalty payable can be appealed against by the taxpayer. FA 2007, Sch 24 para 15

The taxpayer will not be liable for actions taken on his behalf by an agent where he can show that he took reasonable care to avoid an inaccuracy or failure. FA 2007, Sch 24 para 18

Where a return is incorrect because a third party has deliberately provided false information or deliberately withheld information from the taxpayer with the intention of the return being incorrect, a penalty can be charged on the third party, whether or not the taxpayer is charged a penalty in respect of the same inaccuracy. FA 2007, Sch 24 para 1A

The taxpayer may be charged a penalty for the same inaccuracy if they did not take reasonable care to ensure the information supplied by the third party was correct. However, the total of the penalties charged cannot exceed 100% of the potential lost revenue (increased maximums apply for errors in relation to category 2 and 3 territories). FA 2007, Sch 24 para 12(4)

There is a “double jeopardy” rule preventing a penalty being charged in respect of an inaccuracy or failure where there has already been a criminal conviction. FA 2007, Sch 24 para 21

11.19 Partnership Self-Assessment

When a partnership is first formed, it must be registered immediately with HMRC by the nominated partner. In addition to registering the partnership, each individual partner (and any subsequent partners) must register individually with HMRC for self-assessment as normal. As part of this process, the individual partners are required to provide details of the partnership which they have joined.

The nominated partner is responsible for completing the partnership’s tax return, which will contain details of the partnership’s profit or loss and other income received by the partnership, as well as showing each partners’ share of the profits and losses on the partnership statement. The partnership itself does not have a tax liability. TMA 1970, s.12AA & 12AB

The filing deadlines for a partnership tax return are the normal self-assessment filing deadlines. Where the nominated partner fails to file a partnership return, every partner who was a partner at any point during the period in respect of which the return is required will be liable to a penalty. FA 2009, Sch 55 para 25

As the partnership return does not show a liability to tax, the tax geared penalties will not apply.

If there is an inaccuracy in the partnership return, each partner will be liable to a penalty for the inaccuracy based on their individual potential lost revenue. FA 2007, Sch 24 para 20

The individual partners will file their own tax returns as normal, and will complete the partnership supplementary pages of the return.
The rules in respect of amendments and enquiries apply as normal in respect of partnership returns. If an amendment is made to a partnership return, corresponding amendments are made to the individual partners’ returns. TMA 1970, s.12ABA(3) & 12ABB(6)

Similarly, an enquiry into a partnership return automatically extends to the partners’ own returns. TMA 1970, s.12AC(6)

Records must be kept by the partnership for at least 5 years and 10 months following the end of the tax year to which they relate.
EXAMPLES

Example 1

Lester received his tax return for 2015/16 on 6 April 2016. He submitted the return to HMRC on 4 March 2017.

What is the final date by which HMRC can give notice of their intention to commence an enquiry into Lester’s return?

Example 2

Kenneth started trading on 1 October 2015. He informed HMRC on 4 October 2016. A tax return for 2015/16 was issued to Kenneth on 19 January 2017.

Kenneth submitted the electronic return on 20 February 2018. His tax liability for 2015/16 was £1,100 of which £100 had been deducted at source.

What is the maximum penalty that may be charged by HMRC for the late submission of the return?

Example 3

Zack is in business as a taxi driver. He submits his tax return for 2015/16 on 29 January 2017. Zack did not want to pay tax on his profits, so he over-stated his petrol expenses by £15,000. He created false invoices to back up his claim. The return shows a trading loss for the year of £(10,000).

HMRC initiate a review into Zack’s return. Zack starts to worry about his excessive claim and decides to disclose the error to HMRC.

Zack has considerable rental income each year and is a higher rate (40%) taxpayer. He has made a claim to set the trading loss against his general income in 2015/16.

State the maximum and minimum penalties that could be charged by HMRC on Zack in respect of his incorrect return.
ANSWERS

✓ Answer 1

The return should have been filed by 31 January 2017 - therefore the return is late.

If HMRC wishes to commence an enquiry into Lester's return, they must send him a notice by the end of the calendar quarter following the anniversary of the actual filing date.

The anniversary of the filing date is 4 March 2018. This is in the quarter ending on 30 April 2018.

The notice must therefore be sent no later than 30 April 2018.

✓ Answer 2

Kenneth has given notice of chargeability within 6 months of the year end (i.e. by 5 October 2016).

The return is issued on 19 January 2017. The due date for filing is therefore the later of:

i. 31 January 2017; or

ii. 3 months from the issue of the return i.e. 19 April 2017.

The return is therefore due on 19 April 2017.

The return was filed on 20 February 2018 which is 10 months late.

The maximum penalties are:

<table>
<thead>
<tr>
<th>Penalty Description</th>
<th>Amount (£)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Initial penalty</td>
<td>100</td>
</tr>
<tr>
<td>Daily penalties (£10 × 90 days)</td>
<td>900</td>
</tr>
<tr>
<td>Tax-geared penalty [5% × 1,000 (W) = £50 or £300 if greater]</td>
<td>300</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1,300</strong></td>
</tr>
</tbody>
</table>

Working

<table>
<thead>
<tr>
<th>Amount (£)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax liability</td>
</tr>
<tr>
<td>Less: Tax deducted at source</td>
</tr>
<tr>
<td>Liability to tax</td>
</tr>
</tbody>
</table>
✓ Answer 3

The potential lost revenue as a result of Zack's error is:

15,000 × 40%  £6,000

Zack's error is deliberate and concealed so the maximum penalty for the error is:

6,000 × 100%  £6,000

However, Zack has made a prompted disclosure, so the minimum penalty for the error is:

6,000 × 50%  £3,000