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Repayment interest

Spring Budget 2023 representation by the Chartered Institute of Taxation

1 Executive Summary

1.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the UK for advisers dealing with all aspects of taxation. We are a charity and our primary purpose is to promote education in taxation with a key aim of achieving a more efficient and less complex tax system for all. We draw on the experience of our 19,000 members, and extensive volunteer network, in providing our response.

1.2 We suggest that the government consults on the rate and approach to repayment interest on overpaid tax.

1.3 The consultation is necessary to identify the changes required to ensure that repayment interest:

a) meets the government's objective to be 'fair and even-handed',

b) provides adequate recompense for the loss of the use of the monies by the business or individual concerned,

c) provides an adequate incentive for HMRC to process repayments in a timely fashion,

d) can (if appropriate), in a predominantly automated fashion, apply different rates of repayment interest to different circumstances (such as delays attributable to HMRC or other types of official error), and different triggers for repayments.

1.4 Unless something is done to bridge the gap between repayment interest and late payment interest, the government will struggle to achieve its objectives of building a trusted, modern tax administration system, that is seen as fair and even-handed. This issue is particularly acute while HMRC is struggling to deal in a timely fashion with many types of tax repayment.

2 About us

2.1 The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.

2.2 The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

2.3 The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries.

2.4 Our members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

3 Introduction

3.1 We are pleased to set out below our rationale for the need to review repayment interest.[1]

3.2 Our stated objectives for the tax system include:

- A legislative process that translates policy intentions into statute accurately and effectively, without unintended consequences.
- Greater simplicity and clarity, so people can understand how much tax they should be paying and why.
- Greater certainty, so businesses and individuals can plan ahead with confidence.
- A fair balance between the powers of tax collectors and the rights of taxpayers (both represented and unrepresented).
- Responsive and competent tax administration, with a minimum of bureaucracy.

3.3 The government's objectives for the tax system are reassuringly similar. For example, the government has committed to build a '*trusted, modern tax administration system*',[2] creating a '*simpler, more transparent framework that helps build greater trust and provides greater certainty for taxpayers*' and a '*tax system that is seen as fair and even-handed*'.

[1] ie on tax overpaid, tax repayable by HMRC etc.
[2] https://www.gov.uk/government/publications/tax-administration-strategy/building-a-trusted-modern-tax-administration-system#the-core-of-a-modern-tax-system

3.4 HMRC's own Charter reflects many of these objectives for trust, transparency and fairness, such as '*being responsive*' and '*treating you fairly*'.[3]

3.5 Generally speaking, HMRC charges late payment interest at the Bank of England base rate plus 2.5%. HMRC pays repayment interest at the Bank of England base rate minus 1%, with a minimum rate of 0.5%.[4]

3.6 As such, there is typically a 3.5% differential between the late payment interest rate and the repayment interest rate. For example, the current late payment interest rate is 6% and the current repayment interest rate is 2.5%. Additional financial sanctions (eg penalties or penalty interest) are also levied on the late payment of tax liabilities. While these were consulted on relatively recently (see later), they compound the unfairness between the recompense for taxpayers, and that for the Exchequer. There are no such financial sanctions on late repayments of tax.

3.7 The government consulted on repayment and late payment interest during 2008 and 2009. This led to the introduction of new provisions within Finance Act 2009; section 101 dealing with late payment interest, and section 102 dealing with repayment interest.

3.8 The need (or otherwise) for differential between the rates was considered, and there were a range of views, with those in support of an equal rate stressing the importance of fairness and adequate recompense. In our own submissions, we recognised the need for differential interest rates, but stressed the need for repayment interest to provide sufficient recompense, particularly in cases of HMRC error or delay.

3.9 While some of the findings from those consultations remain valid, it is right to review whether they remain appropriate some fifteen years on. Further, it would in any event be consistent with the tax policy making process[5] to undertake a review of these changes, particularly considering the current economic and administrative climate. Many businesses and individuals have experienced financial difficulties and have required additional time to pay their tax liabilities (plus interest). Conversely, many businesses and individuals have suffered (and continue to suffer) lengthy delays in receiving repayments from HMRC, even in relation to specific governmental measures designed to improve cash flow.

3.10 While taxpayers and their advisers can submit complaints to HMRC, and seek compensation for costs caused by HMRC's mistakes or delays, there seems to be no provision to reimburse the incremental financing costs, or opportunity costs, of delays in receiving repayments. In any event, making a complaint is a costly and resource intensive process for taxpayers, their agents, and HMRC.

4 Illustrative examples

4.1 We have set out below some simple examples which illustrate the significant differentials that exist between tax repayments / overpayments, and late payments of tax. Amounts are rounded to the nearest £1.

4.2 <u>New interest regime for VAT</u>

[3] https://www.gov.uk/government/publications/hmrc-charter/the-hmrc-charter
[4] https://www.gov.uk/government/publications/rates-and-allowances-hmrc-interest-rates-for-late-and-early-payments/rates-and-allowances-hmrc-interest-rates
[5] https://www.gov.uk/government/publications/the-new-budget-timetable-and-the-tax-policy-making-process/the-new-budget-timetable-and-the-tax-policy-making-process

4.3 Company A submits its VAT return for the quarter ended 31 March 2024 on 30 April 2024, claiming a repayment of £10,000. HMRC makes some enquires into the return, but satisfied it is correct, releases the repayment on 31 July 2024.

4.4 In this instance, HMRC will pay repayment interest of **£58**, calculated at 2.5%[6] of £10,000, for the period from 8 May 2024 (the day after the due date for the VAT return) to 31 July 2024.

4.5 This amount of interest may be wholly inadequate recompense for the delay, particularly as Company A may already have had to pay to its suppliers the VAT on its purchases in the meantime, and thus has to finance the gap between paying the supplier and obtaining the refund from HMRC. If the company's cost of capital is 7%, it is actually still at least £105 out of pocket,[7] so the repayment interest has clearly not provided adequate recompense, even though the company has been fully compliant with its tax affairs.

4.6 Company B submits its VAT return for the quarter ended 31 March 2024 on 30 April 2024, showing a liability of £10,000. The company experiences cash flow difficulties, but makes the payment in full on 31 July 2024.

4.7 The late payment interest will be **£139**, calculated at 6% of £10,000, for the period from 8 May 2024 (the day after the due date for the VAT return) to 31 July 2024.

4.8 So, while Company A is entitled to just **£58** for receiving its repayment nearly three months late (even though it submitted an accurate return, on time), Company B is required to pay interest of **£139**, nearly 2.5 times more.

4.9 The position for Company B is potentially much worse, as it may also be liable to a late payment penalty if it had not (or could not) agree a time to pay (TTP) arrangement with HMRC in a timely fashion. In this case, assuming a TTP had not been agreed, the late payment penalty would comprise two elements; a first late payment penalty of **£400**, being 4% of £10,000 (the full amount remaining unpaid after 30 days),[8] PLUS a second late penalty of **£59**, calculated daily at the equivalent of 4% per annum of £10,000 for the period from 8 June 2024 (31 days after the due date) to 31 July 2024.

4.10 In this case, Company B would be required to pay an additional **£598** by virtue of its late payment, over **ten times** the amount of recompense payable by HMRC to Company A. This imbalance is plainly unfair.

4.11 The government intends to extend this late payment penalty regime to income tax and corporation tax, when they come into the scope of Making Tax Digital.

4.12 <u>Existing interest regime</u>

4.13 Individual A submits their Self-Assessment return for the year 2020-21 on 31 January 2022, claiming a repayment of £5,000 due to the carry back of losses. HMRC do not look at the return for nine months and, after some internal checks, the repayment is made on 28 February 2023, some thirteen months after the repayment return was submitted.

4.14 In this instance, HMRC will pay repayment interest of approximately **£57**, calculated at rates ranging from 0.5% to 2.5%, for the period from 1 February 2022 to 28 February 2023. In the meantime, while the repayment

[6] Assuming the interest rate is the same as today.
[7] 7% cost of capital of £163, less the repayment interest of £58.
[8] Comprising 2% of the outstanding amount at day 15 plus 2% of the outstanding amount at day 30.

is outstanding, Individual A is required to find the funds to make further payment to HMRC in July 2022 and January 2023.

4.15 Individual B submits their return for the year 2020-21 by 31 January 2022, but fails to pay the liability due of £5,000. They pay the outstanding tax in full on 28 February 2023.

4.16 The late payment interest will be approximately **£226**, calculated at rates ranging from 2.75% to 6% of £5,000, for the period from 1 February 2022 to 28 February 2023.

4.17 So, while Individual A is entitled to just **£57** for waiting over a year to receive their repayment, Individual B is required to pay interest of **£226**, around four times more.

4.18 Again, the position for Individual B is actually much worse. Individual B will also be charged three late payment penalties of 5% each.[9] These will add up to a total of £**750**.

4.19 In this case, Individual B would be required to pay an additional **£976** by virtue of their late payment, over **17 times** the amount of recompense payable by HMRC to Individual A.

5 Our recommendation

5.1 It is now twelve years since the government consulted on its general approach to repayment and late payment interest. While the government consulted on harmonising interest rates during 2016 and 2017, the differential between the rates of repayment and late payment interest was not in scope; although we expressed our concerns at the removal of Repayment Supplement for VAT which (prior to its abolition) acted as an incentive for HMRC to issue VAT repayments timeously.

5.2 We suggest that the government consults on the rate and approach to repayment interest on overpaid tax. Such a consultation is necessary to ensure that repayment interest:

a) meets the government's objective to be 'fair and even-handed',

b) provides adequate recompense for the loss of the use of the monies by the business or individual concerned,

c) provides an adequate incentive for HMRC to process repayments in a timely fashion (and a 'penalty' if they do not),

d) can (if appropriate), in a predominantly automated fashion, apply different rates of repayment interest to different circumstances which give rise to repayments (such as delays attributable to HMRC or other types of official error), and different triggers for repayments (such as claims in returns, subsequent error corrections etc).

5.3 We believe that, unless something is done to bridge the gap between repayment interest and late payment interest, the government will struggle to achieve its objectives of building a trusted, modern tax administration system, that is seen as fair and even-handed.

[9] These are levied after 30 days (typically 3 March – the 'penalty date'), five months from the penalty date, and eleven months from the penalty date.

6 Acknowledgement of submission

6.1 We would be grateful if you could acknowledge safe receipt of this representation. We would welcome the opportunity to discuss the issue we have identified and the solution we have proposed in more detail.

The Chartered Institute of Taxation

1 February 2023