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Reform of Behavioural Penalties: HMRC Consultation[1]

Response 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 20,000 members, and extensive volunteer network, in providing our response.

1.2. We agree that the current error and failure to notify penalty regimes are complex, difficult to administer and in urgent need of simplification. They also need to provide stronger incentives for taxpayers to make disclosures and co-operate with HMRC compliance checks.

1.3. The penalty regimes should deter non-compliance for the future too. This does not work well at the moment as taxpayers are generally unaware of the regimes until after they incur penalties. There is nothing in the consultation document which will remedy this situation, so we encourage HMRC to spend time and money on comprehensive, repeated awareness raising if they wish any reformed or new regime to have a deterrent effect.

1.4. The complexity of the current regimes also hinders the effectiveness of the penalties as a deterrent. We support the removal of minimum 10% penalties for inaccuracies disclosed after three years and for failures to notify for non-deliberate behaviour. This should provide more of an incentive for people to come forward to disclose errors or failures to notify and help to enhance fairness and trust in the tax system, whilst shifting the focus more onto cooperation during a compliance check.

1.5. We agree that there is scope for penalty reductions for the type and quality of disclosure to be simplified. It will be important to have a clear definition of 'unprompted' and 'prompted' so taxpayers and their advisers can identify and understand what constitutes a prompt and what does not. Otherwise penalty reductions will be challenging to implement on a consistent and fair basis. We are not convinced that the suggestion of breaking down reductions between 'telling' and 'helping' and 'giving access' will simplify the regime. Arguably, there should be a single reduction for co-operation.

[1] Reform of Behavioural Penalties; HMRC consultation
https://www.gov.uk/government/consultations/behavioural-penalties-reform/reform-of-behavioural-penalties--2

1.6. We agree with the principle that deliberate behaviour should be penalised more than careless behaviour. In our view, the current penalty ranges for deliberate behaviour are appropriate. We are not persuaded that they should be increased.

1.7. We struggle to see that there is any merit in increased penalty levels for continued/repeated errors because we consider this is already built into existing penalty calculations, but if HMRC decide to proceed with further measures in this area this will be making the regime more complicated rather than simpler. This seems inconsistent with other proposals in this consultation which are aimed at simplifying penalties. The method to increase the penalty should therefore be a simple multiplier to avoid complex rules.

1.8. We support the simplification of offshore penalties. The rationale for having higher rates for offshore non-compliance is no longer valid now that there are sophisticated data sharing mechanisms with most overseas jurisdictions. The deterrent effect of higher penalties is also highly questionable. A simplification would be to restrict increased penalties to offshore matters where the behaviour is deliberate and where the offshore territory has not signed up to Automatic Exchange of Information Agreements, like the Common Reporting Standard (CRS), Crypto-asset Reporting Framework (CARF) and digital platform data sharing.

1.9. HMRC should publish figures for each penalty type annually to show how many are charged. There should also be a review of unused or little used penalties to evaluate why they are not being used and to assess whether they should be repealed or to justify why they should be retained.

1.10. We are attracted to the idea of replacing penalty suspension with a 'caution'. We think the other suggestion in the consultation - of automatic suspension with the penalty being reinstated for another mistake (which may be unrelated) - is problematic, albeit well intentioned. It would also be more complex to implement than a caution.

1.11. Our view is that the link between behaviour and penalties needs to be retained because it is an important principle. As such, we do not support stripping back behavioural considerations as is being suggested in the 'alternative approaches' section of the consultation document. We support retaining (but simplifying) the existing regime so that it remains necessary for HMRC to demonstrate careless or deliberate behaviour, so the following comments should be read in that context.

1.12. Combining failure to notify and error penalties in the suggested new 'misdeclaration' penalty has its attractions because there are parts of the existing error and failure to notify penalty regimes that are different, which can cause mistakes by HMRC and others in the penalty process. Ideally the processes and bandings should be changed to be the same. It would be simpler to modify the existing regimes than introduce a brand new one. Also, there is a concern that a combined 'misdeclaration' penalty would be difficult to implement consistently across the different taxes, particularly VAT.

1.13. HMRC suggest a new 'civil evasion' penalty for deliberate behaviour, but it does not appear to us to be that different from the existing penalty structure for deliberate and deliberate/concealed inaccuracies.

1.14. A framework of behavioural based penalties is the right approach and the link between behaviour and penalties needs to be retained, but we also need to ensure that there is an effective mechanism under which the penalty amount is determined. In practice, since Sch 24 error penalties and Sch 41 failure to notify penalties were introduced, this has proven not to be straightforward. Changing any behavioural tests also risks adding legislative complexity as existing behavioural tests are key to the discovery assessment regime.

1.15. Considerable time savings and fewer mistakes could be achieved by aligning the penalty bandings and calculation processes for inaccuracy penalties and failure to notify penalties.

1.16. Whatever changes are decided upon, we recommend that they should be consistent for a protracted period so that taxpayers, their advisers and HMRC become familiar with the rules and processes, and the regime can become established. Changes should only be considered, after further consultation, if there is evidence that the changes are not working as expected or not having the desired effect .

1.17. We do not agree with the proposed non-financial sanctions, not least as they are too draconian and would deter taxpayers from making disclosures and agreeing to deliberate penalties. If they are to be imposed it should only be for cases of repeated deliberate wrongdoing, after the taxpayer has been given a formal written warning of the potential consequences of repeating their deliberate mistakes. Given their potential impact on taxpayers' lives, considerable safeguards must be introduced including requiring HMRC to apply to the First Tier Tribunal (FTT) to impose non-financial sanctions, taxpayers being party to the subsequent FTT hearing so they can put their case and taxpayers being able to appeal the FTT's decision.

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. HMRC's consultation seeks views on options to improve the financial penalties that apply when inaccuracies are found in returns and documents submitted to HMRC (Sch 24 Finance Act 2007) and where taxpayers do not meet their obligations (fail) to notify HMRC of circumstances that affect their tax liability (Sch 41 Finance Act 2008).

3.2. Building on the feedback from last year's Call for Evidence[2], this consultation proposes two different approaches to reforming penalties for inaccuracies and failure to notify:

- Reforming the existing framework: this approach would retain key aspects of the existing penalty system but simplify how penalties are calculated and applied. This could involve reducing the number

[2] The Tax Administration Framework Review: enquiry and assessment powers, penalties, safeguards – summary of responses - 30 October 2024 https://www.gov.uk/government/calls-for-evidence/the-tax-administration-framework-review-enquiry-and-assessment-powers-penalties-safeguards/outcome/the-tax-administration-framework-review-enquiry-and-assessment-powers-penalties-safeguards-summary-of-responses

of penalty categories, standardising how behaviour is assessed, and making the rules clearer and easier to follow.

- Exploring an alternative model: this approach considers a more fundamental redesign of penalties to improve clarity and consistency. It looks at whether a different structure could better achieve fairness, compliance, and deterrence while reducing complexity for taxpayers, agents, and HMRC**.**

3.3. The CIOT's stated objective for the tax system relevant to this consultation 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.

4. Question 1: What are your views on removing the minimum 10% penalties for:

1. **inaccuracies disclosed after 3 years?**
2. **failures to notify disclosed after 12 months for non-deliberate behaviour?**

4.1. This would be a welcome and sensible move. The 10% minimum penalty is unfair and creates mistrust in the tax system as HMRC apply this rule even if a taxpayer comes forward immediately that they realise their mistake, if it occurred 3 or more years previously. Taxpayers cannot be expected to correct inaccuracies they are not aware about, nor to notify chargeability when they did not know they were chargeable, within an arbitrary 3-year period.

4.2. Because of its arbitrary nature, the rule does not always reflect the complexity or context of the taxpayer's affairs. For example, some taxpayers only discover issues during a review or on seeking professional advice, often several years after the event.

4.3. It acts as a disincentive to come forward where the error is historic and the taxpayer would otherwise be cooperative. It means that taxpayers who make careless/non-deliberate mistakes and whose disclosure is prompted have almost no incentive to co-operate with HMRC as the reduction for the quality of disclosure is only 5 percentage points (15 + 10 = 25; the maximum is 30).

4.4. Removing the minimum penalty should therefore provide an incentive for people to come forward to disclose errors or failures to notify and help to enhance fairness and trust in the tax system, whilst shifting the focus more onto cooperation during a compliance check. There is more of an incentive for taxpayers to come forward to disclose voluntarily if there is an upside to doing so, ie no penalty. Similarly, it is always easier for advisers to encourage clients, or potential clients, to come forward when there is the possibility of no penalty being charged.

4.5. The minimum 10% penalty for inaccuracies corrected and disclosed after 3 years is in HMRC's guidance[3], not in legislation, so removing it would be simply a matter of withdrawing the guidance.

[3] CH82465 This guidance has been in effect since 5 September 2016.

4.6. In terms of incentivising people to come forward, we also refer to the suggestion we made in our response[4] to HMRC's recent consultation 'New ways to tackle non-compliance' that a general statutory requirement to correct within a specific period of time once a taxpayer becomes aware of a mistake in their tax affairs could help increase the number of taxpayers who proactively rectify errors and omissions, thus reducing the number of nudge letters or compliance checks that HMRC would need to issue. This would reinforce the Professional Conduct in Relation to Taxation (PCRT) requirement on agents to encourage and assist clients to make full disclosures or resign from acting for them if they do not.

5. Question 2: What are your views on the ways in which HMRC could:

1. simplify penalty reductions for unprompted disclosure?

2. simplify penalty reductions for the quality of disclosure?

5.1 **Penalty reductions for unprompted behaviour** – If a careless error/non-deliberate failure to notify disclosure is unprompted then the minimum penalty should be nil with full co-operation/quality of disclosure, as now. This is an important principle which contributes to incentivising voluntary compliance so must be retained.

5.2 However, this is a difficult area as the two terms ('prompted' and 'unprompted') are imprecisely defined and inconsistently applied by HMRC. Thus, they potentially lack the effect to change behaviour and, if the taxpayer feels that the HMRC caseworker unjustifiably treated their case as prompted, they damage trust in the tax system. Also, they risk becoming even more muddled as HMRC increase the use of pop-up prompts (for example, in their tax return software, in the HMRC App and digital tax accounts), circulate messages on social media, issue educational nudge letters and so on. In our view these sorts of prompts should not be treated as 'prompts' for penalty purposes. Instead prompts should be defined as something that happens only after a person files a tax return (for inaccuracy penalties) or the deadline to notify passes (failure to notify penalties).

5.3 This makes HMRC's suggestion of first applying a set reduction to the maximum penalty based on whether the disclosure was prompted or unprompted challenging to implement on a consistent and fair basis, unless and until the words 'prompted' and 'unprompted' are clearly defined and understood by taxpayers, their advisers and HMRC caseworkers.

5.4 In our view, a disclosure should only be treated as prompted if HMRC initiate an enquiry/compliance check or otherwise notify the taxpayer in writing that HMRC have reason to believe that there has been an inaccuracy or failure to notify. This will make the question of determining whether a disclosure is prompted or unprompted more objective and easier to determine both for HMRC and taxpayers.

5.5 With regard to One to Many (nudge) letters, HMRC should allow responses to count as an unprompted disclosure if the taxpayer registers for a disclosure process (eg Contract Disclosure Facility (CDF), Digital Disclosure Service (DDS) or one of the bespoke disclosure services that HMRC offer) within, say, 60 days of the date of the letter and then submits their disclosure within the deadline for the process that they registered for. If the person posts a letter to HMRC with a disclosure in it within the 60 day timescale then this should also count as unprompted. This would provide an incentive for people to disclose and encourage more people to respond to the letters. In essence, such disclosures should be treated the same as those that are started by the taxpayer without hearing from HMRC first.

[4] The Tax Administration Framework Review – new ways to tackle non-compliance: CIOT response 17 January 2025 see para 16.4 https://assets-eu-01.kc-usercontent.com/220a4c02-94bf-019b-9bac-51cdc7bf0d99/927cf209-b33a-405b-a051-23a1cee6993b/250117%20TAFR%20new%20ways%20to%20tackle%20non-compliance%20-%20CIOT%20response.pdf

5.6 Discussions took place at HMRC's One to Many Compliance Advisory Board (OCAB) during 2021/22 on the meaning of nudges and prompts in the context of HMRC compliance activity, particularly with regard to their One to Many letters. What was learnt from this exercise may also be of some help in the context of this current consultation.

5.7 The concept that if a person discloses something unrelated to the matter that HMRC are asking questions about (or are visiting about) then the disclosure is unprompted, must be retained. We note that this is an area where there are often disagreements between advisers and HMRC. However, it is an important principle which encourages more proactive disclosures to HMRC.

5.8 A fixed percentage reduction for an unprompted disclosure— as suggested in the consultation document - would improve consistency, reduce the scope for subjective interpretation, and incentivise early engagement with HMRC.

5.9 An alternative simple method could be to calculate the penalty and then halve it (or charge only 25% of it) for unprompted disclosures. The discount for unprompted needs to be significant to encourage people to come forward and to create a positive impression such that if someone makes a second mistake a few years later then they remember the discount and come forward quickly to rectify the second mistake.

5.10 **Penalty reductions for the quality of disclosure -** HMRC's suggestions in the consultation are complex and not easy to understand. In our view, they would not simplify the regime. Arguably, there should be a single reduction for co-operation. It is artificial to try and break this down into 'telling', 'helping' and 'giving access'. It is notable that the existing legislation does not assign separate percentages to each of these three elements and that the percentages noted in the consultation paper result only from HMRC practice. It is simpler and fairer to look at the overall picture in relation to co-operation.

5.11 There are elements of the pre-2007 penalty regime[5] which could be drawn upon as arguably that system was simpler to apply than the 2007 and 2008 regime. The pre-2007 regime permitted penalty reductions for disclosure, cooperation and seriousness (note that the seriousness part is already covered by the behavioural characteristics). HMRC could reinstate disclosure (does the person make a full disclosure) and co-operation (how well do they co-operate ie helping HMRC by supplying information in good time).

5.12 If 'telling' and 'helping' are merged into a single criterion standardised weightings (eg applying increments of 10%) would reduce ambiguity and promote equitable treatment. However, on the other hand, it is arguably not ideal for HMRC to tie themselves down to only operating 10% increments if this is not provided for in the legislation. HMRC should supplement any change with examples to guide agents and taxpayers in understanding how disclosures are assessed. These comments are only relevant if the suggestion in para 5.11 is not adopted.

5.13 HMRC should not reduce the mitigation they apply to a penalty where they (HMRC) break their own guidance by issuing a formal information notice where a person has a good reason for not being able to provide information to HMRC within HMRC's timeframe and has requested an extension. This disproportionately damages trust and perceptions of fairness.

[5] https://www.gov.uk/government/publications/compliance-checks-self-assessment-and-old-penalty-rules-ccfs15/information-about-compliance-checks-for-self-assessment-and-old-penalty-rules-ccfs15

5.14 If rules on quality of disclosure in Sch 24 FA 2007 and Sch 41 FA 2008 are changed, HMRC will need to check other penalty legislation that use similar mitigation approaches (eg MTD penalties; enabler penalties eg para 8 Sch 20 FA 2016) and replicate the new rules across all of them.

5.15 New penalty regimes tend only to apply from a date in the future. This is because tax geared penalties are effectively criminal due to Human Rights rules and the general principle that criminal offences should never be introduced retrospectively – otherwise people could be convicted for doing something in the past which was not an offence then.

5.16 This will mean that if any changes are made to these penalties following this consultation, the new regime will apply to future tax years, but the old rules will apply to earlier tax years, for example, we will end up with three different penalty regimes for 20 year disclosures. This is not ideal because it will make the penalty system very complicated to administer and difficult to understand. There will also be costs attached due to it creating additional training needs for both HMRC and tax advisers. Guidance with examples will be needed. This is not to say that the existing rules should not be simplified but simply to point out that by doing so some new complexities will potentially be unavoidably created.

5.17 The overall impact on the level of penalties should be a factor in any decision that is taken to reform penalty reductions, bearing in mind that the driver for this reform is simplicity. If the outcome turns out to be that higher penalties are charged for the same behaviours as now, this will disincentivise voluntary compliance and undermine trust both in the penalty system and HMRC.

6. Question 3: With reference to the existing inaccuracy and failure to notify penalty ranges, what would you consider to be proportionate and appropriate penalty rates for both deliberate behaviour and repeated instances of deliberate behaviour? Which factors should be considered when applying these?

6.1 The government proposes introducing higher inaccuracy and failure to notify penalties for those who intentionally conceal or underreport to HMRC. It is reassuring to note that the current proposal is focussed on deliberate behaviour (not careless behaviour, where we would have greater concerns). We agree with the principle that deliberate behaviour should be penalised more than careless behaviour.

6.2 In our view, the current penalty ranges for deliberate behaviour (20% - 70% for deliberate and 30% - 100% for concealment) are appropriate. We are not persuaded that they should be increased.

6.3 As noted above, a framework of behavioural based penalties is the right approach, but we also need to ensure that there is an effective mechanism under which the penalty amount is determined. In practice, it is not always straightforward for HMRC to evaluate whether the taxpayer's behaviour was deliberate, careless and so on. This is made harder when people do not co-operate with HMRC, so we can understand why increasing deliberate penalties is being considered. However, higher penalties are more likely to further encourage non-cooperation with HMRC's requests for evidence of guilt and increase appeals against penalties too. HMRC have information notice penalties which they can use to penalise non-compliance with formal notices. Higher deliberate behaviour penalties need to be balanced against the real risk of higher penalties contributing to lower levels of co-operation (as has already been seen with offshore penalties – see below).

6.4 Deliberate penalty percentages are already high. If they are increased, they potentially become unaffordable and uncollectable. There is no point charging higher penalties if they are not going to be paid.

6.5 With regard to the proposal to increase the penalty ranges for a repeated error or failure to notify, in our response[6] to last year's Call for Evidence 'Enquiry and assessment powers, penalties and safeguards' we said that we struggled to see that there is any merit in increased penalty levels for continued/repeated errors, because we consider this is already built into existing penalty calculations, but that if HMRC decided to proceed with further measures in this area this would come with certain complexities and requirements for safeguards.

6.6 Higher penalties for repeated errors will be making the regime more complicated rather than simpler. This seems inconsistent with other proposals in this consultation which are aimed at simplifying penalties.

6.7 The method to increase the penalty should therefore be a simple multiplier to avoid complex rules. Perhaps it could work something like - calculate the standard penalty and then (a) multiply by 1.5 for the second repeated error or failure to notify; (b) double it for the third or subsequent repeated error or failure to notify. This also means that the voluntary disclosure discount effectively becomes worth more for repeat offenders, encouraging them to come forward.

6.8 The taxpayer must have previously been put on notice in writing that a future error of the same type could lead to higher penalties for repeated behaviour.

6.9 'Repeated behaviour' will need to be carefully defined. In our view, to operate fairly, penalty escalation should be calculated based on the same error within the same tax regime. For example, an error on a self-assessment return should not lead to an escalated penalty for a VAT error. It would also be unfair to treat a single issue covering multiple years as repeated failures/inaccuracies for these purposes and that multiple inaccuracies uncovered in one disclosure event (potentially covering different taxes and time periods) are not automatically treated as 'repeated' non-compliance unless clear behavioural intent or prior opportunities to correct were missed.

6.10 Whilst recognising that this proposal is focussing on repeated instances of deliberate behaviour, some thought will need to be given to how this would interact with a subsequent careless error. For example, if a taxpayer makes a deliberate error, then subsequently notifies HMRC of a careless error, this should not be subject to a tougher sanction/multiplier, as this would disincentivise taxpayers from reporting errors.

6.11 The timeframe during which the taxpayer is 'on notice' before the penalty is 'reset' will need careful thought. It should be long enough to incentivise compliant behaviour but not so long as to be seen as unfair. HMRC will need to keep records to evidence the 'repeated behaviour' element of the penalties to be able to discharge that burden if the taxpayer appeals against the penalty.

6.12 The level of penalty must not become so great so as to dissuade the taxpayer from coming forward to disclose an error. As noted in our response to Question 1, there is a risk taxpayers will be less inclined to engage with an investigation or disclosure process if they view the penalty they are potentially facing as disproportionate, burdensome or unaffordable. This disincentivises voluntary compliance and makes HMRC's job harder.

[6] The Tax Administration Framework Review: enquiry and assessment powers, penalties, safeguards: CIOT response 9 May 2024 see paras 21.3 & 21.4
https://assets-eu-01.kc-usercontent.com/220a4c02-94bf-019b-9bac-51cdc7bf0d99/4f2e242d-3ab0-42d0-ad8e-9a70538879ce/240509%20TAFR%20-%20enquiry%20and%20assessment%20powers%2C%20penalties%2C%20safeguards%20-%20CIOT%20response.pdf

6.13 'Deliberate' is already well defined in case law[7] so we do not see any merit in codifying what is deliberate, plus it will not help to address the non-cooperation issue. HMRC should use their information powers to seek the information from uncooperative taxpayers and penalise them for not doing that (Sch 36 FA 2008).

6.14 There may be an argument for replacing the term 'deliberate' because it can be difficult to apply in identifying the behaviour that has caused an error. Alternative terms are 'fraudulent' or 'civil evasion' which arguably have a clearer association with very serious non-compliance, albeit the term 'evasion' suggests that there are examples of evasion that are not criminal (whereas the law is clear that tax evasion is a criminal offence).

6.15 We have had mixed feedback about the idea of combining the 'deliberate' and 'deliberate and concealed' categories into one. On the one hand it was felt that this would be a simplification and that there was not that much difference between the two behaviours, but on the other hand there was a view that concealment, such as creating false invoices or putting fake names on bank accounts, makes it harder for HMRC to find the fraud and is a much more serious issue, so higher penalties are justifiable. Having said that, if the two categories are combined, concealment could be treated as an aggravating factor in calculating the level of the penalty.

6.16 If HMRC implement higher penalties for repeated behaviour we would suggest that they scrap their Managing Serious Defaulters (MSD) programme[8]. Higher penalties should serve the same purpose as the MSD programme in deterring deliberate defaulters from returning to non-compliant behaviour and encouraging a shift to compliant behaviour. Plus, we have seen little evidence that the MSD programme has been successful at changing behaviour.

7. Question 4: How could penalties for offshore non-compliance be simplified whilst still acting as an effective deterrent?

7.1 We agree with the comments from the 2024 Call for Evidence that the current offshore penalty rates are unduly punitive and disproportionate. Offshore penalties are much too complex and should be simplified, and some should be repealed altogether. Removing the supplementary categories for offshore non-compliance would considerably simplify the penalty regime.

7.2 The rationale for having higher rates for offshore non-compliance is no longer valid and increasingly difficult to sustain now that there are sophisticated data sharing mechanisms with overseas jurisdictions, such as Automatic Exchange of Information Agreements like the Common Reporting Standard (CRS), whereas the offshore penalty regime 'aimed to strengthen the deterrent against non-compliance where information was harder for HMRC to obtain' (as the consultation notes). It no longer makes sense to treat non-compliance connected to highly regulated overseas jurisdictions differently to the UK. The world has moved on from when these categories were first introduced.

7.3 It also seems odd to penalise taxpayers based on HMRC's access to data. If this was compared to onshore matters, it would be akin to saying penalties in connection with inaccuracies on self-employment profits should be charged at a different penalty percentage, because HMRC cannot access information as easily as it can for an employed person paid under PAYE. Such differences can be distortive – at present an LLP which trades faces

[7] *HMRC v Tooth* [2021] UKSC 17 at [42] – [47] and *C F Booth Ltd v HMRC* [2022] UKUT 217 (TCC) – intentionally making a statement which, at that time, the person knew was inaccurate – they intended to mislead HMRC as they knew HMRC would rely on the document (eg tax return). Deliberate behaviour also occurs where a taxpayer suspects that a document contains a mistake 'but deliberately and without good reason chooses not to confirm the true position before submitting' it to HMRC (*CPR Commercials Ltd v HMRC* [2023] UKUT 61 (TCC))

[8] https://www.gov.uk/guidance/managing-serious-defaulters-msd-programme

very different penalties and assessment time limits on its offshore income compared to a company carrying out an identical trade.

7.4 Taxpayers often consider the level of offshore penalties to be very unfair, thus undermining trust in the tax system. In addition, the offshore penalty regime can be viewed as discriminatory in that it is often non-UK nationals who fall foul of them (due to them being more likely to have a bank account or own property in their home (overseas) jurisdiction).

7.5 The language about a 'deterrent' effect appears to be misplaced. Most people are unaware of the higher penalties until they seek advice on correcting a mistake, so the penalties have little or no deterrent effect.

7.6 Indeed, offshore penalties can be so high that they can actively deter people from coming forward to make a disclosure. CIOT members also report that many clients who need help correcting the position regarding UK tax due on offshore assets,

- hold those assets for purely legitimate reasons (eg bank accounts held / foreign rental of property they lived in prior to their move to the UK), and
- they have simply not appreciated the UK tax system seeks to tax worldwide income/gains on UK residents in the absence of a remittance basis claim (until recently).

7.7 Therefore, any deterrent effect should be linked solely to the behaviour that brought about the loss of tax. In principle there should be no difference in penalty rates for non-deliberate failures irrespective of whether the matter is domestic or offshore as there is no difference in culpability.

7.8 On the other hand, there may be an argument for charging a higher penalty for offshore deliberate inaccuracies or failures to notify where the matter involves an offshore jurisdiction which has not signed up to CRS, or equivalent (eg FATCA), CARF or digital platform data sharing. One simplification therefore would be to restrict increased penalties to offshore matters where the behaviour is deliberate and where the offshore territory has not signed up to CRS (or equivalent).

7.9 The rule could simply be that if the country was in CRS (or equivalent) as an indicator that it is transparent, then the penalty is just the standard penalty. If it is not transparent (ie not in CRS) then the penalty is the standard multiplied by 1.5. This simple penalty uplift may help to deter movements of money to non-CRS jurisdictions.

7.10 Given the large and increasing amount of information available to HMRC from offshore jurisdictions (eg via the CRS, the CARF and digital platform data sharing agreements) it is difficult to justify retaining the 12-year time limits for offshore errors which only apply to IT, CGT and IHT at present. This should be reviewed.

7.11 This review is also an opportunity to identify whether there are any penalties that are rarely or ever used, and if there are, whether there is any evidential reason for them to be retained, and if not, repeal them. For example, we are not aware of HMRC charging asset-based penalties (FA 2016 Sch 22), offshore asset moves penalties (FA 2015 Sch 21), or penalties under the serial tax avoidance regime (FA 2016 Sch 18). If penalties are not being charged, consideration should be given as to why this is the case, and whether they are still needed. Repealing penalties which are never used would simplify penalty legislation and reduce training needs for both HMRC staff and advisers.

7.12 If offshore penalty uplifts are changed it should be noted that it is not only Sch 24 FA 2007 and Sch 41 FA 2008 which would need amending. Offshore uplifts appear elsewhere in legislation eg 12 month late filing penalties. Changes should be replicated across all legislation where offshore uplifts currently apply.

8. Question 5: How could HMRC simplify penalty suspension while retaining an effective prompt to taxpayers to address the source of the inaccuracy?

8.1 In our response[9] to last year's Call for Evidence 'Enquiry and assessment powers, penalties and safeguards' we said that we would favour a regime that does not penalise the first error but puts the taxpayer on notice that any future errors will incur a penalty. Therefore, we are attracted to the idea of replacing penalty suspension with a 'caution'.

8.2 The caution seems more appropriate if simplification is the most important driver. There would be no requirement for a suspension regime which has many challenges, as the previous Call for Evidence found. The use of the word 'caution' is also likely to come across to taxpayers as more official, and easier to understand, than talking about 'carelessness'.

8.3 The communication of the caution will be key but done in the right way it could work well at shaping future behaviour, particularly if it has an educational focus. The message should be one of leniency now because HMRC could have charged a penalty of between X and Y for this mistake but are not going to do so this time. However, there will be consequences for making further, similar errors. HMRC expect you to improve your systems/records etc. If you make another similar error on the same tax in the next X years you will not be offered a caution that time. The caution letter could then be used by businesses to generate internal momentum to implement improved systems.

8.4 Thought is needed as to whether there should be a period of time the caution should exist for and if so, what that should be – perhaps three years. It would not be fair for the caution to last indefinitely. Likewise, it would need to be clear what kind of further error would trigger a penalty to be charged (rather than another caution). The caution would need to be recorded to reduce time spent by HMRC, taxpayers and agents dealing with subsequent inaccuracies and disagreements, so that all parties can deal with any future problems with certainty. It would be far simpler and quicker for HMRC, taxpayers and agents than the current suspension process.

8.5 We think that automatic suspension with the penalty being reinstated for another mistake (which may be unrelated) is problematic, albeit well intentioned. It would be more complex to implement than a caution.

8.6 Automatic suspension could potentially have unintended consequences. It could deter voluntary disclosures of subsequent errors because taxpayers might not want to admit them in the suspension period if it means that the original penalty is then payable on top of a penalty for the subsequent error. In addition, if HMRC do not find the next error for a few years (eg they do not open a timely investigation) then the suspension would stand, incorrectly, and the period during which the suspended penalty would come into charge would have expired.

8.7 HMRC should not introduce random policies (which are not supported by the legislation) to restrict access to suspensions/cautions. A current example is that the digital disclosure process currently requires a taxpayer to submit an offer to pay penalties, alongside tax and interest, where the taxpayer is seeking to suspend the penalties and agree suspension conditions with HMRC. HMRC will only consider suspension on such cases if this offer letter is submitted, despite the fact that HMRC will issue a replacement offer letter when suspension

[9] The Tax Administration Framework Review: enquiry and assessment powers, penalties, safeguards: CIOT response 9 May 2024 see para 19.4
https://assets-eu-01.kc-usercontent.com/220a4c02-94bf-019b-9bac-51cdc7bf0d99/4f2e242d-3ab0-42d0-ad8e-9a70538879ce/240509%20TAFR%20-%20enquiry%20and%20assessment%20powers%2C%20penalties%2C%20safeguards%20-%20CIOT%20response.pdf

criteria are agreed. This is an inefficient process for HMRC, agents and taxpayers (which can deter taxpayers from seeking a suspension, despite the policy intent for suspensions). Also HMRC guidance indicates that HMRC will not suspend a penalty if there is tax avoidance. It is also unclear why the legislation does not allow suspension for failure to notify penalties.

8.8 We also refer to our comments at paras 5.14 and 5.15 of our response to HMRC's consultation 'Closing in on Promoters of Marketed Tax Avoidance' where we highlight emerging problems with the operation of the law in Para 3A Sch 24 FA 2007 (errors related to avoidance arrangements), which deems an inaccuracy in a return to be careless where the taxpayer relied on disqualified advice. However, we are hearing from members that the measure is failing to meet its policy objective and undermining trust in HMRC and the tax system. This is because taxpayers are often unaware that what they are involved in is marketed tax avoidance and consider that they have taken appropriate advice, so to receive a careless penalty seems unduly harsh in these circumstances. We recommend that to address this issue HMRC should automatically suspend penalties charged as a result of Para 3A (or issue a caution).

8.9 We do not support the introduction of a tax awareness course in place of suspension or a caution. There is a big range of taxes and many different types of mistakes. The course would be challenging and potentially costly to administer nationally and it would be difficult to make the course effective and useful. If a tax awareness course were to be provided, like driving offences, it should be optional – ie you could choose to take the penalty instead.

9. Question 6: What do you see as the opportunities and challenges of this approach? How does it compare with potential simplification to existing penalties, as outlined in Chapter 3?

9.1. Our view is that the link between behaviour and penalties needs to be retained because it is an important principle. As such, we do not support stripping back behavioural considerations as is being suggested in this section of the consultation document, but we can see the advantages of simplifying the current regimes. We support retaining (but simplifying) the existing regime so that it remains necessary for HMRC to demonstrate careless or deliberate behaviour, so the following comments should be read in that context.

9.2 Combining failure to notify and error penalties in the suggested 'misdeclaration' penalty has its attractions, not least because the existing regimes do not work well because the penalty calculation methodology for Sch 41 FA 2008 is different to that for Sch 24 FA 2007 – suspension applies to one, not the other for example. The bandings are slightly different. This causes mistakes by HMRC and others in the penalty process. Ideally the processes and bandings should be changed to be the same. It would be simpler to modify the existing regimes than introduce a brand new one.

9.3 A concern is that a combined 'misdeclaration' penalty would be difficult to implement consistently across the different taxes, particularly VAT. Feedback we have received is that failure to notify penalties should be retained for VAT, as this is the simplest way of penalising a failure to register. The proposal is to replace two regimes with two, different regimes. This does not appear to provide the simplification sought and would require considerable costs to implement. It would be simpler to have one penalty regime but implementing this would not be as cost effective as the suggestion in the previous paragraph.

9.4 Furthermore, replacing carelessness with reasonable excuse would make penalty behaviours out of step with discovery. Behaviours are important as they also underpin HMRC's ability to issue normal time limit discovery

assessments. Plus, existing case law on reasonable excuse does not apply to inaccuracies, which could bring about further uncertainty and technical disputes.

10. Question 7: What is your view on HMRC's use of tougher non-financial sanctions to deter and respond to deliberate and repeated non-compliance and to promote future compliance?

10.1. HMRC suggest a new 'civil evasion' penalty for deliberate behaviour, but it does not appear to be that different from the existing penalty structure for deliberate and deliberate/concealed inaccuracies. Perhaps renaming existing deliberate penalties to 'civil evasion penalties' would have the desired outcome? However, given that 'deliberate' is well defined in case law (as noted above), we would not recommend doing this.

10.2. The consultation document mentions lifestyle restrictions, such as travel or driving restrictions, in the most serious cases where deliberate and repeated non-compliance has already occurred. These types of sanctions may be contested under human rights laws. There is a risk that some people would be less affected than others, thus undermining the effectiveness of the sanction. Given the draconian nature of the proposals and their potential uneven effect, we do not support their introduction.

10.3. Appropriate safeguards would need to be put in place given the impact such restrictions could have on a person's day to day life and the fact that the restrictions may also affect their family members. These sanctions should only be issued by the First-tier Tribunal, on application from HMRC, rather than being issued by HMRC. The Tribunal should require HMRC to present evidence supporting that all the legislative criteria are met before they will impose the non-financial sanctions. The person to be sanctioned should be involved in the hearing and should be able to appeal the Tribunal's decision.

10.4. HMRC can already publish details of deliberate defaulters, although we understand that research has shown it not to be particularly effective, not least because there is low awareness of it amongst the general public. It should be scrapped if it cannot be made more effective – HMRC could use the money saved to open more compliance checks.

10.5. More prosecutions for deliberate, repeated non-compliance may have a deterrent effect. HMRC could write to all those charged deliberate penalties warning them that they may be prosecuted if they make deliberate mistakes in future in relation to any tax, setting out the maximum criminal sanction for cheating the public revenue. Education may effectively deter repeated deliberate wrongdoing.

10.6. We support the sharing of more information with regulators and supervisory bodies.

11. Acknowledgement of submission

11.1. We would be grateful if you could acknowledge safe receipt of this submission and ensure that the Chartered Institute of Taxation is included in the List of Respondents when any outcome of the consultation is published.

The Chartered Institute of Taxation

17 June 2025