

Follower notices and penalties consultation: CIOT response

Management of taxes

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The Chartered Institute of Taxation has responded to HMRC's recent consultation, which was seeking comments on proposed changes to penalties for failing to take corrective action in response to a follower notice.

A report (see tinyurl.com/2fnmvnb9) by the House of Lords' Economic Affairs Committee 'The Powers of HMRC: Treating Taxpayers Fairly' (in December 2018) had recommended that the follower notice (FN) legislation be amended to include a right of appeal to the tax tribunal and that the FN penalty regime be abolished. The government rejected the recommendation to abolish FN penalties because this would render the regime ineffective. However, it undertook to examine the possibility of providing greater judicial oversight of the FN safeguards but was unable to identify any options that would not re-introduce or worsen the delay in settlement, which the regime was designed to address. Therefore, HMRC's consultation document focused only on making changes to the FN penalty to try to place a stronger focus on penalising taxpayers with unmeritorious cases who choose to continue to pursue their dispute after receiving a FN, rather than considering wider 'access to justice' issues.

HMRC propose to reduce the standard rate of the penalty from 50% to 30%, but to maintain the higher rate for those taxpayers whose cases are without merit and whose continued refusal to settle with HMRC is deemed to be time wasting. The purpose behind the proposal to reduce the standard rate of the penalty to 30% is to provide a more genuine choice to those taxpayers who believe their own case is different and has a strong chance of success, and therefore who wish to continue to pursue their appeal, instead of taking corrective action.

In our response to the consultation document, the CIOT says that in general we agree with the proposals in the consultation document, in the absence of HMRC

following the House of Lords' recommendations. We are aware that the high level of the current FN penalty (50%) can act as a disincentive for a taxpayer to continue with their appeal even if they consider that their case has a strong chance of success. However, even at a penalty level of 30% we would anticipate that the same issues will remain and that it will still act as a disincentive for a taxpayer who considers they have a strong case to continue with their appeal. In other words, it does not overcome the fundamental problem with the FN penalty regime, which is that it puts pressure on a taxpayer not to exercise their legal rights. We say that in our opinion the proposal to introduce a new 30%/20% penalty structure seems to us like a 'fudge' when what is actually needed is a more radical overhaul to overcome the rule of law problems presented by how the FN regime is formulated.

We go on to consider some alternative options, which might help to achieve a better balance between the objectives of FNs to discourage further litigation of points already settled with the rights of taxpayers to continue a genuine dispute. These include reducing the standard FN penalty to a figure below 30%, perhaps to 25%. A penalty at this lower level would be less of a disincentive for a taxpayer who considers they have a genuinely different case to those that have already been litigated to continue with their appeal. But, we suggested, the penalty would still be at a high enough level to encourage a taxpayer whose case is on all fours with the scheme that has been litigated to take the appropriate corrective action and settle their own case with HMRC, particularly with the threat of the new 20% penalty on top. Another option is that the FN does not apply an immediate penalty, but rather puts the taxpayer on notice that if they do not succeed in the Tribunal, and if the Tribunal issues a costs order on the basis that the taxpayer has acted unreasonably in bringing the proceedings, then they will be liable for a x% penalty. Then, instead, what is penalised is behaviour that is objectively unreasonable (proceeding unreasonably) rather than behaviour that is not unreasonable (disagreeing with HMRC and seeking resolution of the dispute from the Tribunal).

Our response can be found on our website at: www.tax.org.uk/ref748.