

TaxZone Newthwire

Issue 102 - 12 June 2006 - Self-assessment survival guide

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(1) Introduction

It is now over 10 years since self-assessment was introduced. The system has been highly successful for the government and HMRC, as it has transferred the tax assessment and collection functions over to the taxpaying public and brought in more tax and at an earlier date. On the other hand the private sector has had to cope with more complicated administration. In theory at least, staff numbers at HMRC should have decreased substantially, but many staff members have been transferred to compliance and investigation functions.

A principle of self-assessment has been the ability of HMRC to impose automatic penalties for late filing of returns and late payment of tax, and this has been almost 'a licence for HMRC to print money'.

Previous Newthwires that have dealt with this subject, to one extent or another are:

No. 7 - Self-assessment problems – 5 August 2002

No. 56 - Record keeping – 19 July 2004

No. 70 - Self assessment update – 10 March 2005

(2) Computerisation

The passing of the years has also seen the development of computer systems in connection with tax returns, both in the private sector and within the Inland Revenue.

I do not propose to comment on this aspect in detail. However, it is fairly clear that no accountancy practitioner is now able to deal with personal tax returns economically without an in-house computer system to cope with the preparation and submission of returns.

Equally, HMRC have progressed with computer handling of self-assessment tax returns, some aspects of which will be considered later in this wire.

Planning point

Practitioners who still complete clients' tax returns manually should consider and research computer systems to deal with this task.

(3) Statute Law

The underlying statute law regarding self-assessment was considered in detail in previous wires, but the main statutes are:

Sections 8 & 9, Taxes Management Act 1970 - Requirement of the taxpayer to complete and file a personal self-assessment tax return.

Section 9A, Taxes Management Act 1970 - Ability of HMRC to institute a self-assessment enquiry within certain time-limits.

Section 12B, Taxes Management Act 1970 – Requirement of taxpayers to keep detailed business and personal books and records.

Section 19A, Taxes Management Act 1970 – Ability of HMRC to require production of documents in a self-assessment enquiry.

(4) Case Law

Most of the cases that have come before the Commissioners and courts following self-assessment concern enquiries, and many of these have been considered in previous wires. The following are some of the most up-to-date cases:

R (on the application of Murat) v CIR [2005] STC 184

The taxpayer was a chartered accountant who, following a self-assessment enquiry into his affairs, was required to produce specified documents to HMRC, including a balance sheet. His appeal against a section 19A notice was dismissed and various tax penalties were imposed. His further appeals against the original notice, penalties and a breach of the Human Rights Act were all dismissed by the High court.

Low v MRC SpC 510

The taxpayer was issued with a section 19A notice, but appealed, contending that he should not have to produce the same documents that had been produced in connection with an enquiry into his claim for Working Families' Tax Credit. The taxpayer also invoked art. 8 of the Human Rights Act. This appeal failed, on the basis that income tax legislation was a different regime to Tax Credits legislation. Also, the taxpayer had only submitted documents for six months in connection with the Tax Credits enquiry.

Jacques v HMRC SpC 513

The taxpayer had been issued with a section 19A notice, and subsequently penalties for non-compliance were imposed. On appeal the Special Commissioner held that the penalty notice was invalid. However the submission of the grounds of any appeal were mandatory. If the penalty notice had not been validly appealed at the time it could not be appealed against. However, the parties should have liberty to restore the preliminary hearing if they could not agree as to the legal result of the Special Commissioner's decision.

Commane v HMRC SpC 518

The taxpayer underwent a section 9A enquiry, during which a section 19A notice was issued. The taxpayer appealed to the Special Commissioner, who held that the documents and information were reasonably required. Failure by the taxpayer to produce the items within 30 days of the tribunal's decision could result in severe penalties. Had HMRC sought costs in this case, the Special Commissioner stated that he might well have awarded costs against the taxpayer, had an application been made.

(5) Compliance

We now turn to compliance, and how to ensure that both the accountant and his or her clients do not fall foul of the self-assessment legislation and regulations.

(a) Record keeping

Accountants should stress to their clients that 'incomplete records' are no longer acceptable. Either the client must write up his or her books of account, or the books will be written up in the accountant's office, which will be extremely costly. In extreme cases HMRC may impose a penalty of up to £3,000.

Planning point

Recalcitrant clients must be persuaded to keep proper books of account and comply with section 12B, Taxes Management Act 1970.

(b) Form 64-8

Practitioners should ensure that a valid Form 64-8 is in force for all clients, so that neither party receives 'nasty surprises' from HMRC.

Planning Point

A necessary part of office systems is to ensure that a form 64-8 is in force for every client, and operates correctly...

(c) Office systems

Accountants' office systems should be implemented to record tax returns received, the date they are sent to the client for signature, and the date they are submitted to HMRC, with the appropriate tax payment.

Systems should also be put in place to monitor half-yearly payments of tax, and applications for reductions of payments on account.

Planning point

Accountants should institute systems to monitor the date tax returns are received, sent to clients for signature and submitted to HMRC with tax payments. Systems should also embrace half-yearly payments and applications for reductions of payments on account.

(d) Return preparation

Assuming that the accountant delegates most cases to his or her staff, necessary staff training on the (presumably) computer preparation of returns should have taken place. This will need to be backed up by the checking of returns by a senior member of staff.

Some practitioners use an annual questionnaire sent to clients in order to obtain the necessary information and documents. It is essential that personal tax clients are asked the correct questions, either verbally or by letter or email.

Planning point

Tax return systems are vital, if the practice is to be profitable and run smoothly. More junior staff need to be trained in the computer preparation of returns.

(e) The 'White Space'

Each practitioner will have to make up their own mind about the use of the 'White Space' in the personal tax return at Box 23.7, and Box 3.116 for self-employed accounts. Whether or not HMRC officers actually study the White Spaces is immaterial. If the taxpayer has given appropriate information to back up figures in the Boxes and explains entries, then disclosure has been made and no accusation under the discovery legislation at section 29(3)–(5), TMA 1970 can be made. Even if accompanying letters and documents are attached, it is recommended that the White Spaces are fully filled in.

Planning point

It is recommended that full use of the White Spaces in the self-assessment tax return is made, in order to avoid any possible accusation by HMRC of lack of disclosure.

(f) Accompanying documents

It has been traditional for accountants to send the annual accounts and tax computations relating to clients to HMRC with a covering letter. Following HMRC computerisation and self-assessment, the view of HMRC has been that the department wants as little accompanying 'paper' as possible.

One reason for this is that, if the self-employment pages are filled in correctly, then all the figures relating to the accounts and tax computations are available in the boxes of the return. The other reason is that it is understood that when clients' returns are received by HMRC, this is at a 'receiving centre' and all accompanying enclosures are detached from the return and are placed in a 'shoe box'. The implication is that perhaps not all the documents will reach the inspector or other HMRC officer who actually reviews the return.

Practitioners will have to decide how little attachments or how many they supply with each return. Personally I fill in the White Spaces of my return, but also include a covering letter and copies of my accounts and tax computations.

Planning point

Each accountant will have to decide which enclosures and how many are submitted with each client tax return.

(g) Filing

The next stage is actual filing of the return. This may be by electronic means or by hard copy in the post. If the latter method is adopted, some simple checks need to be made. Has the return actually been signed? Have all the relevant boxes been completed? Are all the necessary attachments with the return? Is the return addressed to the correct HMRC address?

It must be remembered that, particularly when returns are filed at the last minute prior to 31 January, then simple failures of this type could result in an automatic late filing penalty if the form is returned to the accountant or taxpayer.

The report by Lord Carter into self-assessment and other matters has come as a big shock to the professions. He has recommended that from the year 2008, all hard copy returns should be filed by 30 September following the end of the tax year, rather than 31 January, and electronic copies should be submitted by 30 November. This is, of course, only a recommendation, but if adopted will cause huge

administrative problems for the accountancy and taxation professions. Planning of work will have to be re-assessed, and the use of staff between 1 October and 5 April replanned.

At present practitioners have to plan return submission. In theory this can be staggered throughout the tax year, and it will be possible to file some returns before 30 September, allowing HMRC to make the tax calculation. Human nature being what it is, however, many clients will wait until the last minute to provide their books of account and tax information. This leads to a 'bulge' in work around the end of the calendar year and in January.

This problem has been a frequent source of discussion on AccountingWEB. Some commentators suggest that, if clients produce their books and accounts at the last minute, then they should have to pay the fee in advance. Alternatively, or in addition, a much higher fee should be charged if information is provided at the last minute before the 31 January deadline. A radical solution is to 'cull' clients who regular offend in this way.

Planning point

Actual filing of tax returns needs to be planned. Last minute checks are essential. Client education is necessary, in order to avoid the January 'panic'. The situation may get worse if Lord Carter's recommendations are adopted.

(h) Tax payments

Tax is due, for self-employed individuals and partnerships, on 31 January and 31 July. Each practice needs to keep an administrative record so that clients are advised in good time of their agreed half-yearly tax payments and additional amounts at 31 January. It appears that under Lord Carter's report, the date for payment of end of year tax and payment on account for the next year will remain as 31 January. That, at least, is welcome.

In some instances, applications for reductions of tax due in respect of half-yearly payments may be relevant, and this is another area that needs to be dealt with and monitored by the accountancy practice.

Planning point

Tax payments by clients need to be agreed, monitored and in some instances applications need to be made for half-yearly reductions of payments on account.

(6) Enquiries

A principle of the self-assessment system is that, not only has the taxpayer and his or her adviser taken over the work of HMRC, but they will also be penalised in the form of penalties, surcharges and interest if they get it wrong!

I do not propose to discuss this aspect in detail, as it has been covered in previous Newthwires, notably most recently in Newthwire No. 92 on Tax Investigations Update. However, practitioners and their clients must be aware that any failure to file on time, provide information correctly and pay on time will be penalised by HMRC in terms of penalties, surcharges and interest.

The concept of 'reasonable excuse' exists, but its application is very limited. At the present time HMRC and the government obtain millions each year from automatic penalties for late filing and payment. This fact needs to be communicated to recalcitrant clients. Long gone are the days when practitioners are prepared to pay automatic penalties on behalf of clients (that is, unless the failure was their fault).

Included in the enquiry regime, which is imposed by section 9A, TMA 1970, is the power of HMRC to ask for production of documents under Section 19A. This controversial power has also been the subject of

previous wires, so I do not intend to repeat myself, but two points are important. One is the time allowed to produce the documents, and the other is the scope of the request by HMRC.

In cases where the inspector is adopting an intransigent stance, possibly unfairly, the taxpayer has the opportunity to apply to the Commissioners for closure of the enquiry under section 28A. This option must not be underrated.

Planning point

Accountants need to be aware of the enquiry regime, and in particular the penalties, surcharges and interest that can be imposed by HMRC. Clients generally need to be made aware of the automatic penalties, surcharges and interest that can be charged for late filing and payment in non-enquiry cases.

(7) Conclusion

The key to a practice being able to deal with self-assessment returns efficiently and profitably must rely on organisation – and computerisation. Partners and staff need to be trained in this area, and important information can be passed on to clients through client seminars.

Planning point

Do not deal with self-assessment on an ad hoc basis. Organise your practice to add value through this aspect of tax, and plan how this can be achieved profitably.

Ask a question

Readers with a current case should post their query in Any Answers.

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