



REFORM OF VAT PENALTIES

HMRC have reformed the VAT penalty system for late submission and payment of VAT returns. This change is aimed at making the penalty system more consistent across all taxes. The new system will apply to VAT accounting periods beginning on or after 1 April 2022.

Background

The current default surcharge system will be replaced by the new points based penalty system. Under the current system the late submission and payment of a VAT return is penalised by a default surcharge which is calculated as a percentage of the tax due on the return. A surcharge liability notice is issued for the first default, and subsequent defaults are successively surcharged at 2%, 5% and 10% up to a maximum of 15% of the tax due. However, the surcharge does not increase according to how late the return is submitted and default interest is not charged.

The default surcharge system has resulted in large disproportionate penalties for businesses who submit their returns late, perhaps due to a simple error. This in turn has historically led to numerous tribunal appeals on the financial penalties issued.

The New Penalty System

The new penalty system will be split between late submission and late payment of VAT returns. The intention is that it will affect those who fail to meet their obligations to provide VAT returns and other information requested by HMRC on time. HMRC will no longer issue an automatic financial penalty for late submissions but will instead issue a certain number of points before a financial penalty is issued. The intention is that this new points-based system should be more proportionate, penalising only those taxpayers who persistently miss their submission obligations rather than those who make occasional mistakes.

Late Submission

HMRC will issue a single penalty point for a late submission of a VAT return and, once the business has exceeded a points threshold for multiple missed returns, a flat penalty of £200 will be imposed for that return and any subsequent late returns.

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The points threshold for penalties will be based on the frequency of submission of the VAT return. They will be set at:

- Annual returns: 2 points
- Quarterley returns: 4 points
- Monthly returns: 5 points

Points will have a lifespan of two years, after which they will expire. However, if the taxpayer has reached the penalty threshold, the points will not automatically expire but will only be reset to zero if two conditions are met:

1. A period of compliance, meeting all submission obligations on time for the period of compliance (see below); and
2. The taxpayer submitted all submissions which were due within the preceeding 24 months. It does not matter whether these submissions were late initially.

The periods of compliance are:

- Annual returns: 24 months
- Quarterley returns: 12 months
- Monthly returns: 6 months

Late Payment Penalty

In addition to the above there will be late payment penalties as follows:

There will be no penalty at all if the VAT is paid late but within 15 days of the due date.

The first penalty is set at 2% of the outstanding amount if it is paid between 16 days and 30 days after the due date.

If there is any tax left unpaid 30 days after the due date the penalty is set at 2% of the outstanding amount at day 15 plus 2% of the outstanding amount at day 30. In most instances this will amount to a 4% charge at day 30.

A second late payment penalty is charged at a rate of 4% per annum, calculated on a daily basis on the total unpaid tax incurred from day 31.

Late Payment Interest

Late payment interest (calculated at 2.5% above the Bank of England base rate) will also be payable on VAT outstanding after the due date for a VAT return.

Where a payment is made after the due date, late payment interest will be payable from the due date until the date that full payment of that tax is received by HMRC.

In order to avoid these late payment penalties, ongoing daily charges and interest charges, businesses who are having difficulty paying should consider approaching HMRC in order to agree a “time to pay” arrangement.

Effect on Businesses

Although this new system appears to be fairer overall, as with all tax reforms there are likely to be winners and losers once this is implemented.

It should be good news for businesses who might occasionally submit and/or pay their VAT return a few days late (less than 15 days) because of an administrative error or short term cash flow perhaps. A payment of less than 15 days late will incur interest which is likely to be relatively small when compared with a default surcharge penalty under the current system.

However, businesses who are struggling to pay their VAT returns at all and are frequently more than 30 days late settling the tax due will find the new system much more punitive. This is particularly the case for the daily penalty imposed once a VAT return payment has been outstanding for more than 30 days.

This is an overview of the new VAT penalty system designed to raise awareness for businesses. Our VAT team would be pleased to discuss your business and provide a view on your VAT efficiency. For an initial consultation to see whether there is a need to consider your VAT affairs in more detail, please contact your usual Rawlinson & Hunter LLP Partner or one of the following:

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The Rawlinson & Hunter VAT consultancy advises on domestic and international transactions. We regard VAT as a key tax for many of our clients, which is why our service in this area is led by highly experienced and senior members of the tax team with a proven track record of negotiation success on a range of VAT matters. Our aim is to provide commercially realistic advice and practical solutions to your VAT problems. We believe that VAT should be an important part of the wider tax planning for most businesses.

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