

New indirect tax penalty regime

On 1 April 2010, new penalties will come into force for failure to notify a liability to register for VAT; the unauthorised issue of a VAT invoice; misuse of a product so that a higher rate of excise duty is payable; supply of a product knowing that it will be misused in such a way, and handling of goods subject to unpaid excise duty.

The penalties regime for VAT will be extended to other taxes (including insurance premium tax, environmental taxes, and excise and gaming duties), with effect for returns or other documents due to be filed on or after 1 April 2010 (for tax periods starting on or after 1 April 2009).

The penalty regime applicable following the introduction of revised HMRC powers, safeguards and deterrents rules is set out in s 97 and Schedule 24 Finance Act 2007. The new regime began by application to VAT and corporation tax, income tax, PAYE, NICs, the construction industry scheme and capital gains tax, for errors in returns or other documents filed on or after 1 April 2009 for tax periods starting on or after 1 April 2008 and is extended to other taxes (including insurance premium tax, the 'environmental' taxes, and excise and gaming duties) under provisions set out in Schedule 40 Finance Act 2008.

Finance Act 2008 also created new penalties where the error in a tax return results from a third party's actions, and this will apply to virtually all taxes (including VAT, income tax, and corporation tax), effective for returns or other documents due to be filed on or after 1 April 2010 for tax periods starting on or after 1 April 2009.

Schedule 41 Finance Act 2008 introduced penalties for failure to comply with an obligation to notify chargeability to tax, unauthorised issue of VAT invoices, penalties for putting a product to a use that attracts a higher rate of excise duty, and handling goods subject to unpaid excise duty, and these new penalties will apply to obligations arising or actions taken on or after 1 April 2010.

HMRC has issued a leaflet concerning VAT and excise wrongdoing- [LINK](#).

Recent experience for VAT

HMRC has begun to impose substantial penalties in relation to innocent VAT errors and businesses have received penalties of up to 30% of the VAT in question where HMRC considers that there has been a 'failure to take reasonable care' in collation and submission of VAT returns. VAT traders have also received penalties calculated on the amount of VAT by which claims for

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repayments of VAT were considered by HMRC to have been overstated, where the claim is considered to be overstated due to 'failure to take reasonable care'. Schedule 24 Finance Act 2007 provides that penalties must be considered for inaccuracies in documents (i.e. returns and claims) and this also includes documents likely to be relied on to determine repayments. More specifically, a penalty is chargeable where a person gives HMRC a document which is inaccurate and which leads to a false or inflated claim to repayment - if the inaccuracy was 'careless' at the time of submission.

The implications of this for future returns, declarations and claims across the spectrum of HMRC-administered taxes is potentially significant, with the risk of being open to a penalty challenge where HMRC alleges that 'reasonable care' was not taken. Businesses need to consider a high degree of objectivity when filing returns and claims for all taxes on or after 1 April 2010. HMRC has already demonstrated its intent to issue penalties even in circumstances where a mistake is understandable and the result of a genuine misunderstanding or error. It seems likely that the new penalty regime will be implemented across all taxes on a similar basis.

When HMRC is considering issuing a penalty, it will send a written notification. This needs to be taken very seriously as HMRC is giving the taxpayer an opportunity to set out whether or not it took reasonable care in the submission of the return in question. An unhelpfully worded response could provide HMRC with enough information to issue a penalty which it is then difficult to get reduced or set aside.

Excise duty

Excise duty has never had a formalised penalty regime. At present, HMRC can only issue a £250 civil penalty per offence for errors such as failing to submit returns. However, with effect from 1 April 2010, HMRC will have the power to issue, in addition to assessments, penalties based on a percentage of the excise duty at stake and that is likely to greatly increase potential penalty amounts.

The new penalty regime for VAT was introduced in April 2009 and our experience is that, after a transitional period where HMRC monitored issues without acting, it is now more proactive in issuing punitive penalties for even understandable errors. It is therefore of vital importance that all revenue traders who produce, store, move or otherwise deal in excise goods (including businesses that buy alcoholic beverages on the 'grey market' for future sale at retail or wholesale) consider, in advance, how to act to minimise the risk of being penalised.

The list of potential offences includes submitting a return that contains errors, and so penalties may become due in relation to incorrect payment returns submitted by:

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- spirits producers;
- brewers;
- cider makers;
- wine or made-wine producers;
- tobacco products manufacturers;
- refineries and other hydrocarbon oil producers;
- excise warehouse keepers; and
- REDS agents or principles.

In addition:

1. non-submission or incorrect submission of a warehouse keeper's stock return (form W1) may also be liable to penalties where an excise liability is due, particularly in relation to outstanding Accompanying Administrative Documents (AADs);
2. submission of an incorrect claim for Alcoholic Ingredients Relief is also liable to penalties.
3. a number of excise payment return forms allow companies to offset amounts from the duty payment (spoilt beer, cider, made-wine, destroyed tobacco products, vapour recovery for petrol, for example): any errors in this offsetting calculation will also be liable to penalties.

Therefore, this list of penalties could be applicable to:

- producers of excise goods;
- importers of excise goods;
- warehouse keepers;
- logistics firms who act as agents for importers;
- food manufacturers.

In addition to the penalties attributable to the failure to submit returns, penalties may also be applied to the above type of revenue traders who do not hold the proper approvals to carry on their excise business.

The range of penalties is broad and the actual penalty issued will be open to mitigation but, as opposed to receiving a potential £250 civil penalty for non-submission, late submission or incorrect submission of a payment return, even for innocent errors HMRC will have the power to issue penalty assessments of up to 30% of the excise duty excluded from the return. And for

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errors that are considered to be deliberate or concealed, this figure rises to a maximum of 100% of the duty at stake for dishonesty.

Grey market

Many retailers and wholesalers purchase alcoholic beverages on the 'grey market'. Currently s170A of the Customs and Excise Management Act 1979 relieves any dealer in excise goods from a penalty if he bought the goods in good faith. Unlike VAT, excise duty is not required to be shown on an invoice and it is generally difficult to confirm that the excise duty has been accounted for.

From 1 April 2010, s 170A will be repealed and replaced by a new law linked to the penalty regime.

S 4 Schedule 41 Finance Act 2008 states:

“A penalty is payable by a person (P) where:

(a) after the excise duty point for any goods which are chargeable with a duty of excise, P acquires possession of the goods or is concerned in carrying, removing, depositing, keeping or otherwise dealing with the goods, and

(b) at the time when P acquires possession of the goods or is so concerned, a payment of duty on the goods is outstanding and has not been deferred.”

Section 10 goes on to state that the potential lost revenue, i.e. the amount to which the penalty percentage (between 30% and 100% depending on the circumstances) is applied, is an amount equal to the amount of duty due on the goods.

Although any penalty may be mitigated for disclosure, the current provisions concerning 'due care and attention' have been removed. Therefore, it is very important that retailers and wholesalers review supply chains and suppliers to ensure that excise duty payment has been made on the goods purchased, particularly as HMRC has recently launched its renewed alcohol anti-fraud strategy.

Qualifying end use

Many companies supply, receive and use excise goods duty free or duty rebated depending on end-use criteria. Examples include kerosene or red diesel for heating purposes or off road use,

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tied oils, and duty free spirits (for pharmaceutical use etc). Any person who supplies rebated oil or duty free spirits may be liable to a penalty if the procedures of supply are not robust and the goods supplied by them are used for an ineligible purpose. Similarly, businesses that receive duty free or duty rebated goods (for example, pharmaceutical companies) will be liable to penalties for misuse of those goods.

The products that will be liable to penalties for misuse in relation to supplier and user are:

- duty free spirits;
- imported goods not for human consumption containing spirits, for example if a perfume is imported and the alcohol used in it has not been denatured and is subsequently misused;
- tied oils;
- rebated heavy oil (for example, the use of 'red' diesel for a purpose that should attract the full rate of duty);
- kerosene (used in a road vehicle, for purposes of private pleasure flying, or supplied as heating fuel but misused);
- light oil supplied as furnace fuel but used for another purpose (for example, cement production);
- rebated bioblend or biodiesel; and
- road fuel gas on which no duty has been paid.

The above list covers a broad range of businesses in the UK from the pharmaceutical industry to cement producers, chemical companies to laboratories.

The new rules will become legally binding from 1 April 2010. Therefore, any business that potentially has an exposure (and often, businesses may not be aware that an exposure exists, particularly if the oil or spirits are bought duty free) to excise duty penalties should review the current supply chain, customer data, record keeping procedures when using duty free goods, approvals from HMRC and its general excise compliance procedures.

What must I do?

HMRC's attitude has increased the need for companies to be vigilant, exercise and document 'due diligence' in its tax affairs, and implement compliance procedures which will be followed rigorously throughout the business. Furthermore, it must also be noted that if the company is caught under the Senior Accounting Officer rules, an individual could also be held personally responsible for any incorrect excise duty treatment of supplies.

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4 Eyes Ltd has recently appointed Cedric Andrew as Senior Managing Consultant. Cedric has unrivalled expertise in supply chains for VAT and duty purposes and during his time with HMRC as MTIC National Coordinator, it was Cedric and his team who devised the current alcohol and tobacco strategy and implemented the Know Your Customer which is the only effective defence against penalties and assessments by HMRC in this area. 4 Eyes Ltd can conduct a review of your supply chain and advise where this needs to be strengthened.

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