MAKING TAX DIGITAL: VOLUNTARY PAY AS YOU GO

ICAEW welcomes the opportunity to comment on the consultation paper *Making Tax Digital: Voluntary pay as you go* published by HMRC on 15 August 2016.

This response of 7 November 2016 has been prepared on behalf of ICAEW by the Tax Faculty. Internationally recognised as a source of expertise, the Faculty is a leading authority on taxation. It is responsible for making submissions to tax authorities on behalf of ICAEW and does this with support from over 130 volunteers, many of whom are well-known names in the tax world. Appendix 1 sets out the ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark proposals for changes to the tax system.

We should be happy to discuss any aspect of our comments and to take part in all further consultations on this area.

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The Institute of Chartered Accountants in England and Wales
Chartered Accountants' Hall
Moorgate Place London EC2R 6EA UK
icaew.com/taxfac

T +44 (0)20 7920 8646
F +44 (0)20 7920 0547
E taxfac@icaew.com

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For more information, please contact ICAEW Tax Faculty: taxfac@icaew.com

icaew.com

MAJOR POINTS

Key point summary

1. We welcome the fact that the government has listened to the responses to the December 2015 discussion document on simpler payments and is proposing no change to due dates or payments on account, at least for the current parliament.

2. HMRC should take more time to get the systems and processes right and, in the meantime, promote the current budget payment plan for which take up is very low. Seeking to have voluntary PAYG systems and processes in place for income tax by April 2018 is overly ambitious.

3. If the objective is to have businesses and landlords make payments closer to when the income is earned, changes to the payment on account regime would be a simpler way to achieve this.

4. We are not convinced that there would be significant take up of voluntary PAYG. HMRC has indicated that it has received feedback from businesses in support of voluntary PAYG but in reality many businesses are likely to prove reluctant to pay earlier than they are obliged to. Otherwise they would initially be making voluntary payments at the same time as payments for current liabilities. Many already budget and retain funds in a separate interest earning bank account so that they are available when tax becomes due and will prefer to continue with this approach.

5. Quarterly updates will not be sufficiently accurate to form a reliable basis for voluntary payments. Estimated liabilities based on quarterly updates are likely to differ significantly from the final liability creating queries and reconciliation activity. HMRC should not revisit payments on account to match sums being reported under MTD and we are particularly concerned that consideration is being given to making this mandatory.

6. We are concerned that HMRC would not make repayments quickly enough if and when required. Although HMRC intends to develop a flexible system which would allow voluntary payments to be repaid quickly the necessary controls may inevitably mean that repayments could not be made as quickly as the business might require them. If that happens taxpayers will be very reluctant to use voluntary payments.

General comments

7. We welcome the fact that the Government has listened to the responses to the December 2015 discussion document on simpler payments and is proposing no change to due dates or payments on account. We understand that this assurance is for the lifetime of the current parliament only and are concerned that there could be changes in the next parliament before Making Tax Digital has become well established. Any such changes should be subject to separate consultation.

8. HMRC should take more time to get the systems and processes right and, in the meantime, promote the current budget payment plan which has very low take up. Seeking to have voluntary PAYG systems and processes in place for income tax by April 2018 is overly ambitious.

9. If the objective is to have businesses and landlords make payments closer to when the income is earned, changes to the payment on account regime would be a simpler way to achieve this.

10. We are concerned that HMRC would not make repayments quickly enough if and when required. We acknowledge that HMRC intends to develop a flexible system which would allow voluntary payments to be repaid quickly. However, we would query whether, in practice, such a system is possible. It is likely that such a facility would be targeted by fraudsters and HMRC would have to have controls in place to counter this and the risk of money laundering – would these controls not inevitably mean that repayments could not be made as quickly as the business might require them?

11. A number of members have commented that HMRC would be acting as a quasi-bank and queried whether this would be appropriate.

RESPONSES TO SPECIFIC QUESTIONS

Question 1: Do you see any challenges with the voluntary payments process described? Do you think there are alternative options that should be considered, and if so, what are these?

12. We are not convinced that there would be significant take up of voluntary PAYG. HMRC has indicated that it has received feedback from businesses in support of voluntary PAYG provided that it is flexible and straightforward. In reality many businesses are likely to prove reluctant to pay earlier than they are obliged to. Many already budget and retain funds in a separate interest earning bank account so that they are available when tax becomes due and will prefer to continue with this approach. Alternatively they may use the funds to reduce the interest payable on borrowings. Businesses may not have fully appreciated that on introduction there would be bunching of payments (for profits based taxes, less so for VAT and employer's PAYE) and that they would be making voluntary payments at the same time as payments for current liabilities. Many will simply not have the cash available. See Appendix 2 for some direct quotes from our members. If there was a genuine appetite amongst businesses for more certainty about their forthcoming tax liabilities many more would file early and not wait until shortly before the deadline before filing their self assessment return.

13. Quarterly updates will not be sufficiently accurate to form a reliable basis for voluntary payments. Estimated liabilities based on quarterly updates are likely to differ significantly from the final liability creating a lot more queries and reconciliation activity. Payments on account are poorly understood by taxpayers and adding estimated quarterly liabilities into the mix will create more confusion – this needs much more consideration before implementation. There is an inherent simplicity to the concept of filing a return and paying the tax due per that return which may get lost.

14. Universal credit awards are based on net income after tax; it is not clear how voluntary payments would be treated for universal credit purposes.

15. The proposal that payments and repayments under voluntary PAYG will be made electronically will disadvantage those who cannot interact digitally and an alternative channel should be made available.

Question 2: Do you have any views or suggestions on the display of voluntary payments in the digital tax account?

16. The examples shown in the consultation document would be very difficult for taxpayers to follow (agents less so because they have the necessary skills). Fundamentally this is due to an increased number of transactions all in one account which makes understanding statements more difficult however well-presented in the digital tax account. We would question whether estimated amounts and voluntary payments should be shown in the tax account alongside amounts which are legally due and payments that have been allocated; estimates and voluntary payments could be shown elsewhere so that businesses have a clear picture of what is actually due.

17. HMRC appears to be making the assumption that having all taxes shown in one account will aid understanding. This will not necessarily always be the case and there will be businesses where responsibility for VAT, for employer's PAYE and for Income or Corporation Tax rests with different departments, individuals and even different agents. An option to keep the different taxes separate should remain available with an overall picture also being shown.

18. It is difficult to comment in writing on the display of information in the digital tax account; this would be better done in a workshop environment with some models to act as a basis for discussion. We would be pleased to assist with the detailed design.

19. It is not clear whether the "one place" in which liabilities would be shown would be the business tax account or the personal tax account. One assumes that VAT, employer's PAYE and corporation tax would be shown in the Business Tax Account. It is not clear where income tax liabilities, which may be based partly on income from self-employment or a partnership and partly on income from other non-business sources, would be shown. This fundamental issue needs to be resolved at an early stage in the design.

20. The display of interest charges and credits in digital tax accounts is particularly challenging as they are calculated on a daily basis but shown on the account at much less frequent intervals. This will be even more challenging if HMRC is regularly offsetting amounts repayable against amounts due for another tax. We do not have an immediate solution to offer but would be pleased to assist with work on this issue.

Question 3: Should there be a 'period of grace', and if so, what period would be appropriate to allow for separate payment of an amount becoming due?

21. A "period of grace" would seem to be an unnecessary complication. A straightforward allocation of payments against liabilities on the date they become due (not before) would be much more straightforward. Unallocated credits should be held as such until that date and not allocated to estimates (any tagging should be limited to an indicator that the payment is a voluntary one and should not be repaid unless requested by the taxpayer). The taxpayer should have the option of allocating payments against specific liabilities, in accordance with common law principles.

Question 4: Do you have any general comments to make on the allocation of voluntary payments?

22. One of the concerns expressed by our members is whether HMRC systems will be capable of allocating payments correctly. There is still widespread incredulity from employers and agents that three and a half years after the start of PAYE RTI, HMRC systems (both core RTI that handles FPS data and ETMP that handles payments) still display unfathomable figures. In recent weeks, earlier years which previously reconciled suddenly seem to have gone wrong. In a number of cases, agents have been told to file earlier year updates to correct HMRC's figures as there has been a data problem at HMRC's end. Naturally, members are very unwilling to "correct" data which is already correct by filing fictitious amendments just to correct HMRC's computer records. ICAEW's response to HMRC's *PAYE RTI post implementation review (ICAEW REP 163/16)* contains further details. Although this submission was made in April 2016, comments received during the last month from members who are employers and payroll agents reveal that the accuracy of HMRC's records has not improved. We recommend that HMRC publishes the PAYE RTI post implementation review as soon as possible.

23. Under common law a creditor can choose to allocate a payment only if the debtor does not themselves specify the allocation. The consultation document appears to ignore this long established principle – the allocation process must be in accordance with the law and allow taxpayers to allocate payments against specific liabilities.

24. Debt Management often pursues withholding type taxes (VAT and employer's PAYE) more promptly and actively than profit based taxes and some businesses therefore prioritise payments accordingly. Is it now HMRC's view that all taxes are on a par when it comes to payment and collection and that there should be no facility for businesses to prioritise paying particular taxes?

25. Allocation of payments across all taxes will only work successfully if the interest and late payment penalty rules are fully aligned.

Question 5: Do you foresee any problems with HMRC's intended approach to the allocation of voluntary payments?

26. Protection of entitlement to benefits is an important consideration – the change to the method of collection of Class 2 and 4 National Insurance contributions has not been straightforward with multiple discrepancies between the information held in the self assessment and NPS databases. The process for early payment of Class 2 contributions to ensure entitlement to Maternity Allowance is not currently working well. It is too early to assess the impact on claims to contributions based Employment and Support Allowance but it is likely that some potential claimants will lose out by not paying their Class 2 contributions by 31 January following the end of the tax year (under the previous system they were likely to have paid by monthly direct debit). Current indications are that the government intends to abolish Class 2 National Insurance contributions and reform Class 4 to make it contributory and that these changes would take place from April 2018, just as MTD for income tax is expected to be introduced – we suggest that this timing clash be avoided.

27. Any deviations from the basic allocation rules will add complexity and will be difficult for businesses to understand. Student loan repayments have been mentioned as another complication that needs to be considered.

28. When a time to pay agreement is made between a taxpayer and HMRC one of the usual conditions is that future tax payments are made as they fall due; it is not clear how this requirement fits with the proposed approach to allocation.

Question 6: What improper or inappropriate use of the repayment facility do you think there may be, and what rules do you think should be applied by HMRC to stop that happening?

29. It is sadly inevitable that the repayment facility will be targeted by fraudsters and there may be inappropriate use such as money laundering. We have not identified any particular rules or procedures to prevent this. Making repayments to the debit/credit card and, if possible, the bank account whence original payments were made may help.

Question 7: Do you agree with a restriction on repayment shortly before a liability becomes due, and if so, what period or terms of restriction do you think should be put in place?

30. We do not agree with a restriction on repayment shortly before a liability becomes due. Until that date the funds belong to the taxpayer and they should be entitled to use them in whatever way they choose. Crown preference was specifically removed in The Enterprise Act 2002.

Question 8: Do you have any views or evidence on whether, and how, HMRC should revisit the sums paid as payments on account to match more closely to the sums being reported under MTD?

31. We strongly oppose the revisiting of payments on account to match them to sums being reported under MTD and we are very concerned that consideration is being given to this being made mandatory. HMRC accepts that quarterly updates will generally be on a cash basis and that tax and accounting adjustments need only be made annually – it would be unacceptable to mandate adjustments of payments on account to match quarterly tax estimates which are not a reflection of annual taxable profits.

32. The consultation document says that a discrepancy between the amounts payable based on the previous year's liability and the real time estimates from updates already submitted will give a conflicting message. It is much more likely that estimated tax liabilities based on quarterly updates will give misleading messages.

33. HMRC has indicated in the consultation document *MTD: Bringing business tax into the digital age* that it intends to offer choice over whether tax and accounting adjustments are made at the time of each quarterly update or only with the end of year activity and declaration. Mandating the basing of payments on account on quarterly updates would effectively remove that choice; businesses would have no option but to make these adjustments quarterly.

34. For many businesses the payments on account based, as at present, on the previous year's liability will provide a more accurate estimate of the eventual liability. This would apply, for example, to businesses that have significant tax and accounting adjustments to make, to seasonal businesses and to the self-employed and landlords who have other sources of income which they report annually.

35. We think it unlikely that the majority of businesses will have submitted their end of year declaration by the date of the second payment on account on 31 July after the end of the tax year. For the 2.5m businesses with periods of account which align with the tax year that would allow a very short period for them or their agents to file the end of year declaration.

Question 9: Do you have any views or suggestions on customers' ability to elect for overpayments to be held as voluntary credits?

36. We support the introduction of an option which allows taxpayers to elect for HMRC to hold overpayments as voluntary credits; taxpayers should be able to withdraw this election whenever they choose.

Question 10: What are your views on how voluntary payments might work for partnerships? Do you think partners will see the convenience of direct payment towards their total liabilities as outweighing a loss of a limited amount of confidentiality?

37. In many cases partners would not want to give up confidentiality for the sake of convenience. The main exception is where there is an appointed agent (which might be a separate partners' affairs department) that handles the tax affairs of the partnership and the individual partners and is trusted to maintain confidentiality. Such partnerships will generally already have arrangements in place to make tax payments on behalf of individual partners and we think it would be best to leave the arrangements to the partnership and the partners.

Question 11: Do you think there are any special considerations that should apply to third party voluntary payments?

38. We are not aware of any reason why third party voluntary payments should not process normally. The considerations are around money laundering and security and there should be transparency about how any subsequent refund would be made.

Question 12: What additional processes or measures would make customers feel more confident about making voluntary payments?

39. We expect that take up of voluntary payments would be low. Our members have indicated they would not recommend voluntary PAYG to their clients and take up would be limited to less than 5% of clients. The clients who would take it up would generally be those who are particularly anxious not to owe money to HMRC rather than problem payers.

40. Advising clients to retain funds to meet their tax bill is an important part of the advice which members in practice give to their clients. Many encourage the use of a separate interest earning account for this purpose and this approach would continue to be preferred to making a voluntary payment to HMRC. Alternatively the taxpayer may use the funds to reduce the interest payable on borrowings. We consider that it would be unacceptable for government, HMRC or an agent to encourage taxpayers to disadvantage themselves by paying money early to HMRC rather than use it to earn interest or reduce interest payable on borrowings.

41. There are three major reasons why agents will not recommend voluntary payments:

- the fact that there is currently no intention to pay interest on unallocated credits. Payment of interest would probably encourage take up but it would be difficult to set an interest rate that provided an incentive but did not result in HMRC effectively becoming a banker accepting deposits.
- concern over how quickly HMRC would, in practice, be able to make repayments as explained in paragraph 10.
- the experience of allocation of payments and repaying overpayments under PAYE RTI as explained in our response to question 4.

Question 13: Do you have any suggestions for the basis on which earlier repayments could be reasonably claimed?

42. The main area where there is demand for earlier repayment relates to the Construction Industry Scheme – both contractors and sub-contractors – and we suggest that the possibility of earlier repayments be considered.

43. We suggest that HMRC reconsiders the policy which prevents claimants of Job Seekers Allowance from claiming refunds of PAYE deducted earlier in the tax year. There is a similar issue with PAYE deductions from some pensions where the taxpayer cannot claim the refund until after the end of the tax year.

44. We are not aware of any other particular demand for earlier repayment but agree that in the example of Research and Developments tax credits, earlier repayment could help to support companies making such investments where cash flow is critical.

45. As noted in the consultation document it would not be appropriate for most claims to be made until the figures for the full tax year are known. This is not currently a priority area and so we have not focussed on it – we would be pleased to consult our members on this specific issue at an appropriate time.

Question 14: Please tell us if you think there are any other costs or benefits not covered in the summary of impacts, including any detail you may have.

46. We have not identified any other costs or benefits.

APPENDIX 1

ICAEW TAX FACULTY’S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.

2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.

3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.

4. Easy to collect and to calculate: a person’s tax liability should be easy to calculate and straightforward and cheap to collect.

5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.

6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.

7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.

8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.

9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.

10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see via http://www.icaew.com/en/about-icaew/what-we-do/technical-releases/tax).

APPENDIX 2

Direct quotes from members on voluntary PAYG:

1. Surely we will be able to count on the fingers of one hand those individuals that want to voluntarily make payments on account? Much better for the business to put the amount into a deposit account until due, unless HMRC is to pay interest.
2. Why would any businessman pay a liability before it is due? It is bad business practice!
3. Taxpayers are used to paying when they get a bill. Voluntary payments and online payments are alien to some.
4. Why would any sane tax payer make voluntary payments? I would never recommend this to any client and would not expect any sane taxpayer would want to do this!
5. No benefit for this unless they paid say 5% tax free interest on any credits! That would be business-like and then some taxpayers would put up with revenue rubbish.
6. Voluntary PAYG - whilst HMRC is seen as an organisation under stress, unable to deal with all relevant information appropriately, it would be seen as high risk to pay in advance or by DD.
7. No benefit to pay early.
8. Less than 20% will take up voluntary PAYG - in practice I am thinking less than 10%.
9. Less than 5% for those likely to take up voluntary PAYG.
10. HMRC systems cannot be trusted. Always only give them money when it is due!
11. Small businesses would benefit on pay as you go, but trying to explain this to clients may be "difficult".
12. I put less than 20% for take up of voluntary PAYG because to say none seemed too definite – will be less.
13. Those who want to pay early already do so in my experience - HMRC hear what they want to.
14. Voluntary payments - less than 20% is actually very few, probably 5%.
15. If there isn't the incentive of HMRC paying credit interest as now hardly any of my clients will pay ahead of due date.
16. Incentives for voluntary PAYG - assurances that the allocation system will work (unlike the current PAYE/NI system) and interest on early payments.
17. I already have a couple of clients who pay monthly into the SA account to build up for their tax payments.
18. If there is no intention of paying credit interest on the voluntary payments, would not the business keep them in their own account where they are receiving interest and have the flexibility of using it in the business more readily if it is needed.
19. In the absence of a significant “carrot” to incentivise businesses to take up the option of, effectively, putting cash on deposit with HMRC to meet future tax liabilities as they fall due, it seems unlikely that many taxpayers will take up the option to do so! Those who budget carefully for such liabilities are likely to seek out the best return on their cash - whether that be placing it on some form of commercial deposit or, more often probably, utilising it to reduce business borrowing and the related interest costs. It seems unlikely that HMRC would be able to, or would wish to, compete with commercial deposit takers, whether it is by offering a commercial rate of interest on sum paid ahead of the crystallisation of the tax liabilities, allowing some form of discount on the tax liability to recognise the early payment or some other form of incentive (putting the money into premium bond type draws, for example).
20. At first sight, the idea to incentivising taxpayers to put cash aside with HMRC to meet future tax liabilities seems a good one. However, there needs to be as much focus on the economics of the idea (from the taxpayer’s perspective) as there has already been on the mechanics of it.