HMRC - CFM99030 - Administration: Penalties: The Three Levels Of Inaccuracy And Penalty For An Incorrect Return

TIOPA10/SCH7A/PARA30(5)

The lowest level of inaccuracy is careless inaccuracy. In this case the penalty, as a percentage of notional tax, is 30%, before any reduction under PARA33.

This rises to 70% for a deliberate inaccuracy that is not concealed, and 100% for deliberate inaccuracy that is concealed.

The inaccuracy is concealed if the company makes arrangements to conceal it, for instance by submitting false information to support an inaccurate figure - para. 27(1).

Should there be an inaccuracy in a return that was not a careless or deliberate inaccuracy at the time the return was submitted, this will be taken to be a careless inaccuracy if the company or person acting on its behalf discovers the inaccuracy, but fails to take reasonable steps to inform an officer of Revenue and Customs of it - PARA31(2).

Guidance is given on what is careless inaccuracy, in the context of the main penalty provisions in FA 2007/Sch. 24 at CH81140. In law, “careless” is viewed as a failure to take reasonable care. Reasonable care can be defined as the behaviour which is that of a prudent and reasonable person in the position of the person in question. For instance, in the FTT decision in

“That penalty applies if the inaccuracy in the relevant document is due to a failure on the part of the taxpayer (or other person giving the document) to take reasonable care. We consider that the standard by which this falls to be judged is that of a prudent and reasonable taxpayer in the position of the taxpayer in question.”

A reporting company will not be aware of a careless inaccuracy at the time a return is submitted - if it was so aware, this would constitute deliberate inaccuracy. A careless inaccuracy could arise, for instance, from the failure to have adequate systems and controls in place. Note, however that inclusion of estimated information in a return is permitted and therefore would not be careless inaccuracy so long as identified, as required by PARA27(2).

An inaccuracy that results from a reasonable interpretation of a provision of the legislation, or a careful application of the legislation to a factual scenario should not normally result in a penalty - see CH84540 for guidance on what constitutes reasonable care, in this context. However, taxpayers should not rely on an interpretation of the legislation being regarded as reasonable if that interpretation makes the legislation incapable of achieving its objective.

An example, whether or not careless inaccuracy

From time to time scenarios will arise where it may be difficult to decide how the legislation should be applied.

By way of example, the definition of a group is based on IFRS accounting. It may not always be clear how a matter might be dealt with under IFRS where, say, US GAAP is applied in a group’s consolidated accounts.

For instance, a substantial private equity group holding company may hold the shares in a number of sub-holding companies for groups. It may be unclear whether the holding company would be regarded as an investment entity under IFRS 10-28, and whether the interests in the sub-holding company should be regarded as investments held at fair value and, therefore, not line by line consolidated (see CFM95350). If the holding company is not an investment entity, it will be the ultimate parent of a worldwide group containing all the sub-holding companies and their subsidiaries. But, if it is an investment entity, and the sub-holding companies and their subsidiaries are not line by line consolidated, each sub-holding company will be the ultimate parent of a smaller worldwide group.

It is possible that there would be no disallowance on the basis of a single large group, but an enquiry into a return leads to the conclusion that there are a number of groups. The original reporting company is a member of a smaller group to which Condition B in TIOPA10/SCH7A/PARA45(7) applies - see CFM98820 - and HMRC issues a closure notice setting out the revised membership of that group, and a total disallowed amount greater than zero. (HMRC would also appoint reporting companies for the other sub-groups’ worldwide groups, to the extent that they contain UK group companies, under PARA49)

As far as the original reporting company’s group is concerned, there is an inaccuracy meeting condition A in PARA26(2), and so a penalty could arise if that was considered a careless inaccuracy.

Suppose the reporting company or, say, the US GAAP reporting group’s parent, sought advice from a suitably qualified adviser on what actions were required by the group to comply with the interest restriction legislation. The group was advised that it was correct to file a single return for a worldwide group, including all the members of all of the subgroups. This advice proved to be incorrect. The inaccuracy here would not be careless, because the reporting company (or a person acting on its behalf in the form of the US GAAP parent) had taken reasonable steps to ensure accuracy by seeking advice from a suitably qualified adviser. This should be the case even if the advice was that the conclusion on the point was finely balanced. This would be a case of a reasonably arguable view of a situation that was subsequently not upheld - see CH81130.

If the group engaged the advisor to give advice and then prepare the return, PARA26(6) would come into play, so that there would not be a careless inaccuracy; the reporting company would have taken reasonable care to avoid the inaccuracy.

If the group simply filed its return, without taking any advice and dealt with the issue wholly in-house and in so doing failed to consider the question of the composition of the group, the relevant legislation and manual guidance, this could be considered as careless inaccuracy, particularly if there were other errors in the return, suggesting a lack of care by the reporting company in developing adequate systems for preparing tax returns.

Finally, if the group acted on advice that where the identity of a group was uncertain, and therefore the total disallowed amount was automatically zero, this is advice which a prudent and reasonable taxpayer should be reluctant to accept: it would be inherently unlikely that this should be a reasonably arguable position. An inaccuracy arising from relying on such advice, without taking steps to check it, would amount to a careless inaccuracy.

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