HMRC - CFM99057 - Administration: Penalties: Special Reduction Where Notional Tax Exceeds Actual Loss Of Tax

TIOPA10/SCH7A/PARA33(7)

The penalties under TIOPA10/SCH7A/PARAS 30 and 32 differ from normal tax-based penalties within FA07/SCH 24 in that they are based on the “notional tax” computed in accordance with PARA30(5) rather than “potential lost revenue” (FA07/SCH7A/PARA5, CH82150). Accordingly, it is possible that the notional tax exceeds or is likely to exceed the actual loss of tax to the Crown that would have arisen from the inaccuracy. This is most likely to be case where there are losses or other reliefs available to UK group companies in the worldwide group that might lessen the loss of tax attributable to the inaccuracy.

Where a reporting company claims that this is the case, a realistic approach must be taken to estimating the actual loss of tax. The group has a great deal of flexibility in arranging its affairs and will normally have 36 months after the end of a period of account to file a revised interest restriction return and statement of allocated interest restrictions or reactivations. (See CFM98780 in relation to amendments of an interest restriction return during the course of an enquiry.) PARA72 extends the time limit for consequential claims in company tax returns on completion of an enquiry CFM98880. The estimation of the likely loss of tax should take into account the entire picture: not only the direct impact on the tax payable by UK group companies for relevant accounting periods that overlap the worldwide group’s period of account, but also the consequential effects on earlier and later periods of account.

For instance, if it is claimed that tax losses would reduce the additional tax payable by a UK group company in consequence of an inaccuracy in a corporate interest restriction return, there are three issues that need to be addressed:

Is there consistency between the computation of the UK group company’s tax position with and without the correction for the inaccuracy? For instance any available tax losses should be taken into account both with and without the correction.

The estimation of tax on one company (taking into account losses and other claims) should take into account the consequential effects of losses or relief being used to cover the effects of the correction on liabilities of that company or other UK group companies in the same, earlier or later period of account. As a rule of thumb it should be appropriate to consider the impact of losses or reliefs in any previous period to which carry-back might have been available and to look at the estimated position for three future years. This three-year look forward reflects the 36 month period in which the group can finalise its position; once that 36 month period has passed, the group should have a reasonable idea of its tax position three years forward and its ability to use losses and reliefs carried forward.

A difference between actual or likely loss of tax and the notional tax will only justify a special reduction in penalty where it is substantial and, in particular, sufficiently large that, in the absence of the special reduction, the strict application of PARA 30 or 32 would produces a result that is contrary to the clear compliance intention underlying the law, see CH170600.

A special reduction arising from an excess of the notional tax over the actual or likely loss of tax is specific to the Corporate Interest Restriction. Accordingly where it is considered that an adjustment is required, or where a reporting company contends that one should be made for this reason only, the officer of Revenue and Customs handling the case must refer it to:

Corporate Interest Restriction Product Owner, HMRC Business Assets and International, Financial Products Group.

If there are other reasons for considering such a reduction, authority is required from TALA (Tax Administration Litigation and Advice, Process Design & Excellence) who will calculate the level of the reduction, see CH175000.

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