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CONFIDENTIAL

PRIME MINISTER

LATE PAYMENT OF VAT

In the Budget, the Chancellor announced his intention to implement most of the recommendations of the Keith Report on Late Payment of VAT. The history is as follows.

In 1980 the Chancellor established a Committee under Lord Keith of Kinkel to report on all aspects of the Inland Revenue and Customs and Excise enforcement powers. The Committee reported in 1983. On VAT, Keith was concerned at the extent of late payment. In the normal way traders have use of the money which has been paid by their customers in VAT for 2¹/₂ months. VAT returns were made quarterly and so the average time VAT is retained by the trader is 1¹/₂ months. In addition the trader has a further month to pay tax after submitting his return.

Keith found that three quarters of all traders were paying late and that arrears totalled around £1¹/₂ billion. He felt that the existing criminal penalties were excessive and, as a result were not being applied effectively. He therefore recommended that civil remedies be introduced, with an interest penalty on tax not declared and a surcharge for tax paid late.

The Government issued a consultation document in July 1983 and reported the results to Parliament in early 1984. The PAC strongly supported the Keith approach. The Government issued a further document in November 1984 setting out its conclusions but asking for comments by January 1985. Thus there have been two rounds of consultation. Following the second round modified proposals were published in the Finance Bill. A rising surcharge is to be imposed where tax is still outstanding more than one month after the VAT return should have been made. This starts at 5 per cent for tax one month

late rising to 30 per cent for tax six months late, by which time the trader will have had use of the VAT money for $8\frac{1}{2}$ months. As a response to the consultations, the Finance Bill includes an escape clause which provides that the trader will not be liable to the surcharge where he has shown due diligence in submitting his return or has a reasonable excuse.

The effect of the measures is estimated to be an increase in annual revenue of £50 million as a result of more accurate returns. In addition there could be a once and for all return in the cumulative arrears of £600 million.

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24 April 1985