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PRACTICE NOTE

PN 112/05

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Income Tax Return Penalty

Introduction

This Practice Note outlines the amendments to the submission dates for income tax returns and the introduction of fixed penalties for late submission. It sets out the statutory submission dates in different circumstances, the consequences for failing to file a return and the suspension of the requirement to file a return in certain cases. It is derived from the Income Tax (Amendment) Act 2004, referred to as the 2004 Act, and the relevant sections are noted. Where it amends the Income Tax Act 1970 (referred to as the 1970 Act), the amended section is noted.

If, having read this guide, further information is required please contact the Income Tax Division at the above address, telephone number, or email address.

Scope

This Guide only considers the returns relating to non corporate taxpayers who are liable to pay income tax in the Isle of Man. For the purpose of this guide non corporate taxpayers are:

- Individuals who are resident on the Isle of Man; or
- Individuals who are not resident but receive income taxable in the Island;
- Trusts, settlements and partnerships.

Commencement

The amendments to the 1970 Act and the introduction of new measures that are considered in this Practice Note shall have effect from **6 April 2005**, in respect of the return of income for the year ended 5 April 2005 and subsequent years. Returns for the full year and part year ended 5 April 2005 will be the first returns affected by the new rules.

Submission of Returns:

- i) Every person who is liable to pay income tax is required to make and deliver a return in respect of the year ended on 5 April. [1970 Act s62]
- ii) Ordinarily an annual return form is issued by the Income Tax Division during the month of April following the year of assessment to which the return relates. These returns will carry the issue date of 6 April.
- iii) Where a return is required, the onus is on the client to make a return. Penalties, etc. that are considered later within this document are not avoided where a return is required but the return has not been issued or received. If it is believed that a return is required but one has not been received then please request a return by contacting the Income

Tax Division.

- iv) The submission of an annual income tax return is required by 6 October following the year of assessment to which it relates. [1970 Act s62]
- v) There are certain situations where the return does *not* carry the issue date of 6 April. The due date is then 6 months after this issue date. Both dates will be clearly marked on the return form.
- vi) Following the death of an individual a return is required for the period beginning on 6 April before the date of death and ending on the date of death. The return will carry the issue date of the actual date the form is issued to the personal representative of the deceased.
- vii) There are specific provisions that relate to cases where an individual ceases to be regarded as a resident on the Isle of Man. These rules require an individual to make a return in respect of the period ending on the date of departure from the Isle of Man and requires that the return is filed no later than 6 months after that date of departure. In this case, the return will carry the issue date of the **date of departure**, and the due date is 6 months after this date. [1970 Act s62a]
- viii) Non-resident individuals, or trusts and settlements ceasing to be liable to Manx Tax - depending on whether the client has informed the Division of the change of circumstance, the submission date will be 6 months after the return form issue date, which may be part way through the year, or 6 April.

Failure to make and deliver a return

[1970 Act s111C to 111I]

First Penalty

[1970 Act s111C]

- i) In the majority of cases, the first penalty will be triggered when the income tax return remains outstanding after **6 October** (ie for the year ended 5 April 2005, the first penalty will be triggered on 6 October 2005).
- ii) For clients commencing residence or leaving school, the Division should be notified as soon as possible. Failing to do this will **not** stop the first penalty being triggered if a return has not been received by 6 October following the end of the tax year.
- iii) For clients ceasing residence during the year, the first penalty will be triggered where the income tax return, which relates to the period ending on the date of departure from the Island, has not been received within 6 months from the **date of departure**.
- iv) In the case of a death – after we have been notified, no penalties will be issued. However, penalties already issued at the time of death, will need to be paid.
NB: A return covering a **period of estate** will be subject to the first penalty, which will be triggered when the return remains outstanding more than 6 months after the due date.
- v) In the case of non-resident individuals, or trusts and settlements ceasing to be liable for Manx Tax, the first penalty will be triggered if the return has not been received by the due date, which will be 6 October following the year of assessment or 6 months after the issue date, whichever is the earlier.
- vi) Partnerships – although a partnership will be included in the reminder cycle, it will not receive a penalty, as the partners will be issued with the first penalty (where appropriate) as individuals in their own capacity.

Second Penalty [1970 Act s111D]

- i) In the majority of cases, the second penalty will be triggered when the income tax return remains outstanding more than 12 months after the end of the year to which the return relates (eg for the year ended 5 April 2005, the second penalty will be triggered on 6 April 2006).
- ii) For clients commencing residence or leaving school, failing to notify the Division will **not** stop the second penalty being triggered if a return has not been received within 12 month of the end of the tax year to which the return relates.
- iii) For clients ceasing residence during the year, the second penalty will be triggered where the income tax return, which relates to the period ending on the date of departure from the Island, has not been received within 12 months from the **date of departure**.
- iv) In the case of a death – as with the first penalty, once we have been notified, no penalties will be issued. However, penalties already issued at the time of death, will need to be paid. NB: A return covering a **period of estate** will be subject to the second penalty, which will be triggered when the return remains outstanding more than 12 months after the due date.
- v) In the case of non-residents or trusts and settlements ceasing to be liable for Manx Tax, the second penalty will be triggered if the return has not been received within 12 months of the end of the year to which the return relates or within 12 months of the issue date, whichever is the earlier.
- vi) Partnerships – as with the first penalty, although a partnership will be included in the reminder cycle, it will not receive a second penalty, as the partners will be issued with the second penalty (where appropriate) as individuals in their own capacity.

Examples of First and Second Penalties

- i) Full year returns:

Income Tax year ended	5 April 2005
Return issue date	6 April 2005
First penalty triggered on	6 October 2005
Second penalty triggered on	6 April 2006

- ii) Full year returns – late notification of a liability:

Income Tax year ended	5 April 2005
Notification of liability made on	6 November 2005
Return issue date	7 November 2005
First penalty triggered on	6 October 2005 (*)
Second penalty triggered on	6 April 2006

(*) 6 months after the end of tax year, the issue date of the return has no effect.

- iii) Part year returns (e.g. following cessation of residence):

Residence ceased on	5 November 2005
Notification of cessation of residence	5 February 2006
Return issue date	5 February 2006

First penalty triggered on	6 May 2006	(*)
Second penalty triggered on	6 November 2006	

(*) 6 months after the date residence ceased, the issue date has no effect.

Estimates on returns and requests for default assessments

Please refer to PN 113/05 - Initial Income Tax Return Penalty – Estimates and Requests for Default Assessments.

Alteration to ITIP Codes

When a return has been outstanding for more than 2 years, it will be considered that a valid claim for deductions and additional allowances has not been made, and therefore deductions such as mortgage and loan interest and life insurance, and Additional Personal Allowance will be removed from the code. The code will continue to include personal allowances (single allowance, married allowance or wife's allowance) and the Blind Person's Allowance/Disabled Person's Allowance where applicable.

Amount of the civil penalties

1. The first penalty has been set at £50 for 2005/2006.
2. The second penalty has been set at £50 for 2005/2006.

The amount of the penalty can be amended for subsequent years with the agreement of Tynwald. [1970 Act s111G]

Mitigation of Penalties

[1970 Act s111E]

- i) The first civil penalty can be mitigated in two ways:
 - a. Automatically – if, having been charged under the first penalty rules, a return is filed and an assessment is raised with a liability that is less than the amount of the penalty; the penalty will be automatically reduced to an amount equal to the tax assessed. Therefore if the assessment liability is £30 - the first penalty will be reduced to £30.
 - b. Other cases – the Assessor or, on appeal, the Income Tax Commissioners may reduce the penalty to an amount (including nil) as may be appropriate.

Notwithstanding the ability to mitigate the penalty, the following factors will not be taken into account by the Assessor or by the Commissioners:

- i. The insufficiency of funds available;
 - ii. That there may not have been a loss of revenue;
 - iii. Acts of good faith.
- ii) The second civil penalty can only be mitigated using the method outlined in point i)b. above.

Reasonable Excuse

- i) The legislation provides for the defence of "reasonable excuse", which must satisfy the Assessor or, as the case may be, the Income Tax Commissioners, before the first and second penalties may be withdrawn. [1970 Act s111F]

- ii) Whilst the legislation does not state what would constitute a reasonable excuse, the Assessor will judge every case on its merits. Situations that may arise include sudden incapacitating illness, death of the taxpayer or close family member.
- iii) Notwithstanding the defence of “reasonable excuse” the following reasons will **not** be considered:-
 - a) Insufficiency of funds available,
 - b) Reliance on another person to perform a task.

Collection of a Penalty

- i) Income Tax legislation provides for the recovery of the penalty in the same manner as if the amount due was a payment of income tax. Therefore, failure to pay the penalty will result in the issue of reminders and, as appropriate, an instruction being sent to the Coroner to enforce payment of the outstanding debt. [1970 Act s111H]
- ii) Having suffered a penalty, the amount shall not be deducted from income or profits that may suffer an income tax charge in that year.

Appeals

- i) An appeal may be considered in respect of any liability to a penalty or with regard to the Assessor’s decision regarding the mitigation of a penalty. The appeal should be made in writing, within 30 days of the date of the notice and should outline the grounds. [1970 Act s111I]
- ii) The Commissioners, on appeal, may confirm, vary or reverse the penalty or the Assessor’s decision.

Criminal Offences

- i) It is an offence not to file an income tax return that is required by current legislation. Whilst initially it is a civil offence not to file a return, legislation provides for a criminal offence, which will be considered in the most serious cases. [1970 Act s111J]
- ii) A criminal offence will be triggered where a return remains outstanding more than 24 months after the date of issue or 24 months after the date on which an individual ceases to be regarded as resident in the Isle of Man.
- iii) Where, following consideration by the Courts, an individual is found guilty of an offence he shall be liable to a fine not exceeding £5000 or custody for a term not exceeding 6 months, or to both.
- iv) Having been convicted of an offence under this part, the individual may also be required to make and deliver the outstanding return.

Suspension from the requirement to file a return

In certain circumstances, a person may only be required to complete a return form on a periodic basis. If this is the case, a letter will be issued at the time that the decision is made. The letter will also advise that, should the person’s circumstances change, the Division should be notified as soon as possible. For further information please see guidance booklet GN30 “Need help with your return form?”

Change of Circumstances

It is extremely important that the Division is made aware of any change in circumstances, eg change of address, marriage, separation, death or leaving the Island, as soon as possible. These changes will have implications for the issue and filing of return forms, as detailed above.

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Assessor of Income Tax

This practice note is intended only as a general guide and must be read in conjunction with the appropriate legislation. It does not have any binding force and does not affect a person's right of appeal on points concerning their own liability to income tax.

Comments and suggestions for improvements of issued Practice Notes and suggestions for future Practice Notes are always welcome.