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Corporation tax: online filing and HMRC's hunger for business data

Corporation Tax: Online Filing

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Donald Drysdale takes a look at the development of CT online filing and examines the new technology standard driving it

The news report that penny-wise former chancellor Gordon Brown had spent £135 on a haircut should have sent a chill down the spine of every tax-compliant barber. With HM Revenue & Customs concentrating these days on Tactical Information Packages and business statistical analysis, surely it will now be only a matter of time before every 'short back and sides' is expected to add an equivalent contribution to turnover.

Some tax practitioners may not have woken up yet to the fact that new approaches to financial and tax reporting will rapidly make them complicit in our new surveillance society.

We are told there are some 5 million CCTV cameras in the UK. Local authorities are adding sound capabilities to many of these, not only listening but also enabling watching officials to bark reprimands at passers by. Trials of new airborne CCTV cameras are adding a new 'spy in the sky' dimension.

In the world of tax, a new technology standard known as XBRL is threatening businesses with similarly intrusive powers by Government authorities. And it is happening by stealth, hidden from most users.

What is XBRL?

'XBRL' is shorthand for eXtensible Business Reporting Language, a relatively new derivative of the XML 'markup language' that has been around since the late 1990s. In a process that has been likened to bar coding of goods, XBRL 'tags' elements of financial data by associating each with a label that identifies its character. It is the product of an international initiative by some 450 multinational business and professional organisations, and in many countries it is already revolutionising financial and statistical reporting by businesses. HMRC is one of the organisations involved.

Like electronic stickers, the XBRL tags describe the data elements to which they are attached in a standard way that can be understood by many different computer systems. Such XBRL descriptors may be added to the components of any set of data to facilitate statistical analysis. While many projects that use this new standard are still in their infancy, the

XBRL implementations that seem most successful to date involve the streamlining of financial reporting systems designed to collect and sift data. Examples are systems used by investment analysts, banking regulators and company accounts filing.

At a high level, XBRL tags may be attached to key figures in balance sheets and income statements. This is already facilitating comparison of otherwise unrelated company accounts by financial analysts and others. More sinisterly, the XBRL labels may be appended to financial data at the transaction level, allowing the tagged accounting data to be categorised and manipulated at any stage after the point of original entry.

We are familiar with the way physical bar codes can assist businesses in monitoring their movements of goods for inventory control purposes. In a some-what similar way, electronic XBRL tags may facilitate multi-dimensional slicing and dicing of transactional data, allowing authorities to analyse it in ways never before envisaged by businesses.

The relevance of XBRL in the context of tax may now be apparent. At first sight it offers no obvious advantage to businesses for tax reporting purposes or to HMRC for simple data collection, but promises amazing new scope when it comes to data manipulation by the tax authority. It would allow HMRC to extract information automatically from multiple sets of accounts, tax returns and computations, comparing figures from each business with those of earlier years, with those from competitors and with industry norms, and flag up those returns that seem to merit further enquiry.

The choice of XBRL for CT online filing

In his report on HMRC's online services, published in March 2006, Lord Carter of Coles recommended that XBRL should be used as the technology format for online filing of corporation tax returns and accompanying attachments by all UK companies. This reflected HMRC's position as one of the large organisations that had helped to create XBRL, but for companies required to e-file their tax returns it seemed to offer few benefits that would not have been available at much lower cost from the simpler and already more established XML standard.

Professional bodies interested in tax have recently questioned the validity of Lord Carter's recommendation. This was triggered, not by a suggestion that it was wrong, but rather by an absence of substantiation that it was right. There was no published evidence that HMRC's decision to use XBRL had been supported by a detailed evaluation and selection process of the kind that might have been expected in a private sector IT project of similar importance.

HMRC is not the only government department showing an interest in this technology. XBRL has already been adopted by Companies House, an agency of the Department for Business, Enterprise and Regulatory Reform, as the basis for its new online filing system that has been commended for its user friendliness. There seems little logic supporting the choice of XBRL for data collection alone, but Companies House is a major purveyor of financial data, selling company information and derived statistical data to third parties. In such a context XBRL comes into its own, facilitating categorisation and analysis of data in ways that could not have been dreamt of with older technology formats.

Although HMRC has not produced the results of a selection process demonstrating that XBRL is the right basis for CT online filing, there are strong pressures within the IT industry suggesting that the XBRL standard will be more and more widely used. HMRC seems unlikely to alter its existing view that 'XBRL is the only show in town'.

Interestingly, this contrasts with the Financial Services Authority, another body that imposes mandatory electronic reporting on a large number of businesses. The FSA observed in 2005 that 'XBRL is not the only option in town' and announced in 2006 that it had decided against adopting it on grounds of cost.

HMRC is currently implementing the recommendations of Sir David Varney's review of links with large business, published in November 2006. In line with these, HMRC's Large Business Service is developing a new risk-based approach to tax compliance which looks closely at businesses' reliance on tax-related systems and processes in an effort to identify those organisations that pose the greatest risks of tax error. This approach is expected to be extended to other large businesses dealt with by Local Compliance.

Computerised analysis of XBRL-based CT returns and accompanying accounts and computations should help HMRC to determine where certain tax risks lie. Where such risks are identified and enquiries need to be pursued, examination of relevant accounting and tax computational data may be swifter and easier where XBRL-tagged data is available, and this may speed up the enquiry process.

In spite of concerns surrounding HMRC's insistence on imposing XBRL-based CT online filing on all companies, there may be some real benefits ahead for tax-compliant businesses. More sophisticated risk assessment ought to focus tax enquiries on organisations that warrant them, and those assessed as having low tax risks should find that they face less intervention from HMRC.

Countdown to mandatory CT online filing

Lord Carter recommended that all companies should be required to file their company tax returns online, using XBRL, and make payments electronically, for returns due after 31 March 2010. HMRC has recently reviewed and extended this deadline. The present position, announced on Budget Day 2007 is that online filing of company tax returns, and use of XBRL for accounts and tax computations, will be required for all companies for accounting periods ending after 31 March 2010 where the return is submitted after 31 March 2011. Paper submissions will not be accepted. Companies will also be required to pay their CT electronically, but this includes bank giro so it should not present any insurmountable difficulties.

Very large businesses with specialist XBRL requirements, such as financial institutions needing to use the new standard for regulatory reporting, may incorporate it into their in-house IT systems, either by tagging individual transactions or at a higher level. In time, XBRL capabilities will also be built into proprietary accounting software and will thus become increasingly available to businesses.

For the majority of companies and their tax agents, the imposition of XBRL for CT online filing will be a transparent process looked after entirely within proprietary accounting and tax software packages. These will produce accounts and tax computations that look just the same as before, but the output transmitted electronically to HMRC (and, where appropriate, Companies House) will contain the necessary XBRL tags needed to meet the statutory requirements.

The process of implementing XBRL presents much greater problems for software vendors, who have until 2011 to build the necessary capabilities into the 800-plus accounting and tax packages currently used in the UK. Most of these packages have no existing e-filing capabilities. Software developers are having discussions with HMRC to establish exactly what will be needed to meet the new requirements.

XBRL, while transparent to many end users, is extremely complex and cumbersome to program. Software vendors face exceptional costs in meeting the new standard being imposed by HMRC, and software costs can be expected to rise accordingly. Even more worrying is the prospect that some vendors may not manage to update existing packages in time, and companies or agents using them may be forced to ditch these in favour of competing products or otherwise risk facing penalties for failing to file correctly online.

HMRC is taking a huge risk, and putting the welfare of companies and agents in jeopardy, by adopting a 'big bang' approach to CT online filing and imposing the new standard on all companies in the same year. This contrasts with Companies House and its phased introduction of XBRL-based e-filing, starting with the simplest cases. HMRC is being urged to adopt a similarly phased approach.

Joint filing with Companies House

The 2005 pre-budget report contained proposals for joint electronic filing arrangements to streamline companies' obligations to file CT returns with HMRC and accounts with Companies House. These were presented as deregulatory, but met with widespread opposition. They offered little in administrative convenience because most companies submit abbreviated accounts to Companies House and much more detailed information to HMRC. They were also unpopular because they involved accelerating the deadline for submission of CT returns -- currently 12 months after the accounting date.

Acceleration of the CT filing date was abandoned, but the Government removed a disincentive to early tax filing by changing the period within which HMRC could open an enquiry into a company's tax affairs. For non-group companies this period now ends 12 months after the actual date of tax filing. By making this change the Government hoped that companies would be encouraged to use the new HMRC/Companies House joint filing facility when it becomes available by 2011. In the meantime the possibility of an earlier CT filing date is one that ministers have committed to keeping under consideration.

The future

We started with a haircut, but end with more hair-raising possibilities. HMRC is keen to apply its risk assessment and enquiry procedures in real time so far as possible, and the Government may follow the example of others (eg. in Germany and the Netherlands) by giving the tax authority the right to obtain direct online access to business accounting records. Where large businesses have implemented XBRL at a transaction level for their own internal purposes, this could give HMRC greatly increased access to information. It could also put sensitive competitive information at greater risk of leakage than hitherto.

Government interest in XBRL seems to go much wider than HMRC. In spite of the decision by the FSA not to adopt XBRL, there appear to be moves to use the new standard to support more extensive data sharing amongst multiple government departments; for example, HM Treasury plans to use XBRL data from HMRC to achieve better informed modelling in considering policy objectives. Given the Government's questionable record in managing successful IT projects, this raises a variety of serious concerns. In particular, major security issues have been raised by other large scale data sharing propositions such as those addressed by the National Health Service or national identity cards.

Most company tax personnel and tax agents won't wish to get involved in the depths of XBRL and may never have to. However, they should take note of its possible impact on HMRC's future methodology and on potentially wider data sharing by government. They should also plan early to ensure that they are able to meet the mandatory CT online filing demands they will face from 2011 onwards.