14 August 2026

Requiring payment of VAT and PAYE – Direct Debit

Response from ICAS

Requiring payment of VAT and PAYE – Direct Debit

About ICAS

1. The Institute of Chartered Accountants of Scotland ('ICAS') is the world's oldest professional body of accountants. We represent over 24,000 members working across the UK and internationally. Our members work in the public and not for profit sectors, business and private practice. 12,000 of our members are based in Scotland and 10,000 in the rest of the UK.

2. The following submission has been prepared by the ICAS Tax Board. The Tax Board, with its five technical Committees, is responsible for putting forward the views of the ICAS tax community; it does this with the active input and support of over 60 committee members. We have also received feedback from the ICAS Insolvency Committee on the proposals in this consultation.

3. ICAS has a public interest remit, a duty to act not solely for its members but for the wider good. From a public interest perspective, our role is to share insights from ICAS members into the many complex issues and decisions involved in tax and regulatory system design, and to point out operational practicalities.

General comments

4. We welcome the opportunity to respond to the HMRC consultation – Requiring payment of VAT and PAYE – Direct Debit.

5. We do not support the introduction of a requirement for all businesses to pay by Direct Debit for VAT and PAYE at present. The consultation notes that it is a minority of taxpayers that currently pay late. Requiring all businesses to use Direct Debit, even where it is not the payment method best suited to their circumstances, would be disproportionate and likely to cause problems for many businesses.

6. Feedback we have received indicates that many businesses are aware that they could pay by Direct Debit but have good reasons for choosing to pay by other methods. Crucially, businesses want to retain control over the timing and amounts of payments. Other important factors include being able to make payments from different bank accounts, compliance with internal approval processes and having flexibility in structuring payments within groups of companies.

7. There are also widespread concerns about problems with HMRC's systems and processes and the length of time it can take HMRC to rectify any errors. These concerns would have to be addressed before payment by Direct Debit could be mandated. If HMRC took a large (incorrect) Direct Debit payment this could cause serious cash flow problems for many businesses and in extreme cases could cause a smaller business to fail.

8. As a general principle, if businesses are making payments on time, it should not matter to HMRC how they choose to do this, so imposing penalties for failing to pay by Direct Debit would not be reasonable or proportionate. There are already penalties (and interest) to deter late payment.

9. However, we do see some scope for HMRC to encourage more businesses to adopt payment by Direct Debit voluntarily. It would need to address the issues that currently lead to businesses choosing to pay by other means, including improving its communications and putting in place a robust 'fast-track' process for correcting any HMRC errors. We have also suggested a potential incentive for using Direct Debit payments, that could be offered to smaller businesses to assist with financial management.

10. There will always be some businesses which cannot pay by Direct Debit, for example, those making payments above £20m. There will also be other businesses where Direct Debit is likely to remain impractical, even if HMRC improves its systems to reduce errors. If payment by Direct Debit were to be made mandatory in future, there should also be an 'opt out' available for some businesses, subject to appropriate conditions being met.

Specific Questions

Question 1: Are you responding to this survey as:
- **a business**
- **a representative body**
- **an organisation**
- **an individual**
- **other (please provide details)**

11. The Institute of Chartered Accountants of Scotland is the world's oldest professional body of accountants. We represent over 24,000 members working across the UK and internationally.

Question 2 to Question 9

12. See introductory section ('About ICAS') above.

Question 10: Prior to this consultation, were you aware that you could make VAT payments by Direct Debit?

13. Feedback we have received indicates that many businesses are aware that VAT payments can be made by Direct Debit – but choose not to use Direct Debit for the reasons discussed in our response to Question 12.

Question 11: If you currently pay by Direct Debit or previously have done, what benefits or drawbacks, if any, have you experienced?

14. We have received a limited amount of feedback about businesses which have chosen to use Direct Debit to pay VAT. For the reasons outlined in our responses to Questions 12 and 15 below, many businesses prefer to use other methods of payment (and some would find it very difficult to use Direct Debit, particularly larger businesses and VAT Groups).

15. However, we understand that for some smaller businesses, with relatively simple arrangements, it can work. It potentially reduces the scope for errors arising from, for example, a business recording the wrong amount when setting up the bank transfer, although clearly this could lead to either an underpayment or an overpayment. In the case of an overpayment, a business which does not use Direct Debit may be able to correct the problem before making the payment.

16. We have also been told that HMRC communications are unhelpful where a Direct Debit has been set up but too late, so HMRC will not take the payment on time. The online VAT account shows that a Direct Debit is in place and instructs the business not to pay by another method. HMRC also fails to notify the business quickly where a Direct Debit payment cannot be taken. We discuss these issues further in our response to Question 38.

Question 12: If you were aware of the facility to pay by Direct Debit but have chosen not to use this payment method, could you explain why?

17. We understand that businesses want to retain control over the timing and amounts of payments. Allowing HMRC to take payments by Direct Debit is perceived as too risky by many businesses because of concerns about HMRC errors and the length of time it can take HMRC to rectify any problems.

18. If HMRC took a large (incorrect) Direct Debit payment this could cause serious cash flow problems for many businesses and in extreme cases could cause a smaller business to fail.

19. We have been made aware of a range of VAT cases where HMRC has pursued amounts that are not due – if HMRC had been able to take payments by Direct Debit, the problems would have been compounded. Specific issues reported to us include:

- Problems with the VAT central assessment process – incorrect amounts not displaced by the return and pursued by Debt Management. We understand that HMRC has identified the cause of the problem, but this may not be fixed for some time.
- Some businesses have problems with incorrect VAT accounts, where amounts cannot be reconciled with returns. Many of these cases remain unresolved.
- There can also be issues with disputed penalties (under appeal) where HMRC allocates payments to these, instead of the amounts in the return – prompting concerns that HMRC would use Direct Debit to take payment, even though the penalties may be removed at the end of the appeal process.
- Similarly, where HMRC has issued protective assessments, we understand that the system should be set to inhibit collection, but again there are concerns that HMRC might use Direct Debit to take payment before the appeal process has been completed.

20. Businesses affected by issues like this, or in some cases businesses that are aware of others experiencing problems, do not choose to pay by Direct Debit. Many businesses, particularly larger ones are happy to pay electronically via BACS or CHAPS, where they retain control over the timing and amounts of the payments.

21. Businesses may have additional reasons for wanting control/flexibility and choosing not to pay by Direct Debit, for example:

    - While many businesses will have one bank account from which payments are made to HMRC, in some cases we understand that payments may be made by different people (often family members).
    - Businesses, particularly larger ones in VAT groups, often have multiple bank accounts and want to retain the ability to choose which bank accounts to use to pay the VAT liabilities. Businesses that operate through different divisions would also want the flexibility to choose to make payments from different bank accounts.
    - Well-managed businesses with temporary cash flow problems (for example, where a large payment is late) may choose to pay a large (business critical) supplier or their staff, ahead of HMRC. Clearly, it isn't desirable for businesses to build up significant VAT and PAYE arrears over an extended period, where there are underlying financial management or profitability issues – see our response to Question 13 - but retaining flexibility to deal with an occasional problem is seen as important. See also our response to Question 38, for a potential incentive for using Direct Debit, which might assist with financial management.

Question 13: The government expects that making payment of VAT by Direct Debit mandatory could deliver benefits for businesses, including greater automation and reduced administrative burden. What benefits, if any, do you expect this change could bring to your accounting processes or wider business operations?

22. One possible benefit of paying by Direct Debit would be that it reduces the risk of missing payments. We understand that this is a factor for some of those who have already chosen to pay by Direct Debit.

23. On a potential wider benefit that might arise from making payments of VAT (and PAYE), we have received the following feedback from ICAS members working in insolvency. However, it should be noted that this feedback relates to struggling businesses – as set out in our responses to Questions 12, 15 and 26, many well-managed and financially sound businesses have good reasons for not paying by Direct Debit.

24. A feature of many insolvencies is the accumulation of significant VAT and PAYE arrears over an extended period. In practice, these liabilities can become a source of informal working capital, allowing businesses to continue trading despite underlying cash flow or profitability issues. Whilst this may provide short-term relief, it often results in larger HMRC debts, poorer returns for creditors and fewer restructuring or rescue options being available by the time professional advice is obtained.

25. One advantage of mandating payment by Direct Debit, could be that underlying funding or business model issues become obvious sooner - leading directors/business owners to seek

advice at an earlier stage. We understand that earlier intervention is generally positive. Where the underlying business remains viable, a range of funding solutions may be available, including overdraft facilities, invoice finance, asset-based lending and other forms of commercial funding. Those options are more accessible before substantial HMRC arrears have accumulated.

26. There may also be benefits from an insolvency perspective. HMRC currently has secondary preferential status in respect of VAT, PAYE and certain other taxes. If HMRC's exposure is reduced through more timely collection of these liabilities, there is potential for increased distributions to ordinary unsecured creditors in insolvency cases.

27. Similarly, HMRC is frequently the largest creditor in formal insolvency proceedings. Lower HMRC debt levels could result in greater engagement from trade and other unsecured creditors and may assist in promoting rescue options such as Company Voluntary Arrangements, where creditor support and participation are critical.

28. However, these potential benefits would only arise if requiring payment by Direct Debit does improve collection and does prompt struggling businesses to seek advice earlier. Businesses which already choose to pay by Direct Debit probably have stronger financial discipline and a better approach to compliance.

29. There is a risk that businesses which are less financially disciplined or have weaker financial controls (and are already struggling with financial management and compliance obligations), will continue to be unable to manage cash flow and pay their liabilities when required to use Direct Debit. The result might be additional administrative challenges for HMRC and further cash flow pressures for businesses already experiencing financial difficulties.

30. Rather than mandating payment by Direct Debit for all businesses, it might be preferable for HMRC to engage with struggling businesses at an earlier stage before significant arrears have been allowed to accrue. Our response to Question 38 also suggests a potential incentive for smaller businesses to use Direct Debit which could assist with financial management. If the government does decide to mandate payment by Direct Debit, we recommend that some businesses should be offered the ability to opt out – see our response to Question 38 which discusses this in more detail.

Question 14: What barriers or impacts, if any, might making payment of VAT mandatory by Direct Debit have on your accounting processes or wider business operations?

31. See our responses to Questions 12 and 15. Making payment by Direct Debit mandatory will cause significant problems for larger businesses (including VAT groups) which have multiple business bank accounts and internal approval processes. They need to retain control over the timing and amounts of payments – and the ability to choose which account(s) to make payment from.

Question 15: If you do have chosen to use methods of electronic payment other than Direct Debit, are there particular benefits in your chosen method of payment that informed a decision to use these instead of Direct Debit?

32. As set out in our response to Question 12, many businesses, particularly larger ones, are happy to pay electronically via BACS or CHAPS. The key difference between these electronic methods and Direct Debit, is that businesses retain control over the timing and amounts of the payments – and can choose which bank accounts to use to make payments.

33. Larger businesses also operate approval controls over large payments, for example, any amounts over a set threshold might require two approvers. These controls would be difficult to maintain for non-regular amounts paid by Direct Debit (and there would be insufficient notice to stop an incorrect debit).

34. More generally, many businesses do not have sufficient confidence that HMRC would consistently take the correct amounts by Direct Debit, for the reasons outlined in our response to Question 12. If HMRC took a large (incorrect) Direct Debit payment this could cause serious cash flow problems for many businesses and in extreme cases could cause a smaller business to fail.

Question 16: Are you currently excepted from submitting VAT returns electronically?

35. We have no comments on this question.

Question 17: What barriers or impacts might you face by making VAT payments by Direct Debit?

36. There are good reasons why many businesses do not choose to pay by Direct Debit (as outlined in our responses to Questions 12 and 15.

37. If the government does decide to mandate payment by Direct Debit, there will need to be some exclusions, for example, for those making payments above £20m. We recommend that some businesses should also be offered the ability to opt out. We discuss this further in our response to Question 38.

38. If the government/HMRC want to encourage wider adoption of Direct Debit payments (or if there is a move to mandatory payment), HMRC would need to take steps to address business concerns.

39. As a minimum, the problems outlined earlier with VAT accounts need to be resolved before businesses are required to pay by Direct Debit.

40. If a requirement to pay by Direct Debit is introduced, HMRC should only take payments by Direct Debit for amounts shown in the VAT return by the taxpayer – not for any other amounts that may be showing on the VAT account. The notice period would need to be longer to give businesses the opportunity to stop an incorrect payment being taken.

41. HMRC will also need to put in place a robust 'fast-track' process for dealing with any HMRC errors and correcting them rapidly. We discuss this in more detail in our response to Question 38.

Question 18: If you have set up a Direct Debit using VATC9 form or on your online VAT account and currently pay VAT by Direct Debit
- **comment on benefits of this method, if any, you have experienced**
- **comment on drawbacks, if any, you have experienced**

42. We have no comments on this question.

Question 19: Are there any particular customer groups (such as disabled people, people of different ethnic groups, age, sex or gender, marital status, sexual orientation, religion or people with or without dependents) likely to be disproportionally affected? If so, please explain how.

43. We have no comments on this question.

Question 20: What, if any, barriers might you face or impacts might you experience on your accounting processes/business if POA instalments were collected by Direct Debit?

44. For POAs, it is not clear from the consultation on what date the Direct Debit payment would be requested, as the due date for payment is the final working day of the month of the POA instalment.

45. Would the extension to three working days after the due date apply to POAs (ie similar to VAT return payments)? If not, this would mean that businesses that currently settle POAs by CHAPS or Faster Payments would be at a cash liquidity disadvantage because the money would have to be in the account three working days before the due date.

46. It is also unclear from the consultation what the position would be for Balancing Payments – again businesses that currently pay by CHAPs or Faster Payments should not be put at a cash liquidity disadvantage if they were required to switch to using Direct Debits.

47. For the reasons outlined in our responses to Questions 12 and 15, Direct Debits would be more challenging to manage for large payments in larger businesses, in terms of approval and accounting processes.

48. A further issue could arise for VAT Groups, where one VAT Group member may need to fund the POA from a specific bank account (which is not the usual bank account). This could arise where a particular transaction related to one company in the group. This presents no difficulty where other electronic payment methods can be used but would be impossible using Direct Debit.

Question 21: What benefits, if any, do you foresee if POA instalments and the balancing payments were collected by Direct Debit?

49. Some businesses might find that payment by Direct Debit reduced the risk of forgetting to make a POA, but this should be a choice, not something imposed on all businesses.

50. However, feedback we have received indicates that some large businesses do not see any benefits in the context of POA instalments and balancing payments. If the government chooses to adopt a general policy of payment by Direct Debit, we recommend that some businesses should be allowed to opt out – we discuss this further in our response to Question 38.

Question 22: If your VAT liability fluctuates above and below £20million within a tax year please explain the typical range, frequency of fluctuation under and over £20million and why this varies?

51. Examples provided to us include:
    - Disposals of large, opted properties (that do not qualify as TOGCs).
    - Payments following a merger or acquisition (which change the VAT payment profile of a VAT Group).
    - Seasonal businesses.

52. These higher payments are not always predictable and could relate to transactions happening near the end of a VAT period. Given the restriction of Direct Debit payments to £20m HMRC would need to warn the business in advance that a Direct Debit could not be collected, with sufficient notice for the business to arrange to pay by another method. It would not be practicable for businesses to be left to make other arrangements at the last minute.

53. If payment by Direct Debit is mandated, it would be preferable to allow businesses with VAT liabilities fluctuating under and over £20m (and those with payments close to the threshold) to opt out (see our response to Question 38 for further discussion of this proposal).

Question 23: Prior to this consultation, were you aware that payments of PAYE could be made automatically by Direct Debit, following an RTI return?

54. Feedback we have received indicates that many businesses are aware that PAYE payments can be made by Direct Debit – but choose not to use Direct Debit for the reasons discussed in our response to Question 26.

Question 24: How do you currently make payments of PAYE to HMRC?

55. We have no comments on this question.

Question 25: If you have previously not paid on time, or paid with an incorrect reference, can you explain why this happened and would Direct Debit would have help prevent this?

56. We have received some feedback which suggests that Direct Debit might help to prevent late payment in certain circumstances. For example, where a third-party payroll provider is late raising payment requests for PAYE.

57. However, we haven't received any feedback indicating that the potential benefit has been sufficient to outweigh the concerns outlined in our response to Question 26.

58. In theory, it seems possible that payment by Direct Debit could remove issues with incorrect references, but it isn't clear that this would be the case in practice. In one of the scenarios outlined in our response to Question 26 below, the employer was providing the correct reference for the payment – but HMRC was reallocating the payment anyway – so in this example payment by Direct Debit would have made matters worse.

Question 26: If you were aware of the option to use Direct Debit but haven't done so, please could you explain why?

59. See our response to Question 12. Several of the reasons for not using Direct Debit for PAYE are similar to those for not using it for VAT. Businesses want to retain control over the timing and amounts of payments.

60. As for VAT, allowing HMRC to take payments by Direct Debit is perceived as too risky by many businesses because of concerns about HMRC errors and the length of time it can take HMRC to rectify any problems.

61. If HMRC took a large (incorrect) Direct Debit payment this could cause serious cash flow problems for many businesses and in extreme cases could cause a smaller business to fail.

62. We have been told about problems for many employers with RTI reconciliations/discrepancies on PAYE accounts - and HMRC requesting payments that do not correlate to the submissions made by the employer. We understand that HMRC also misallocates payments. These issues would have been made worse if HMRC had been able to take payments by Direct Debit.

63. A recent example reported to us involved disputed PAYE penalties. HMRC repeatedly allocated payments to the oldest liability on the account (the penalties under appeal) rather than the amount in the latest RTI return (in line with the payment reference provided by the employer) – and continued to do so for months after it was agreed that no penalties were due. The business had to spend significant amounts of time calling HMRC to get the payments correctly allocated.

64. HMRC's guidance indicates that a Direct Debit cannot be set up to pay penalties (and HMRC should not be trying to take payment for penalties under appeal), but HMRC's system was apparently unable to distinguish between the different items. If a Direct Debit had been in place, it seems HMRC would have taken a large payment for the penalties under appeal.

65. We have also been told about occasions where a Direct Debit is in place, but HMRC has failed to take payment at the correct time. The business makes payment by bank transfer – but HMRC then takes the Direct Debit late and without giving any notice, creating duplicate payments. HMRC's system does not recognise that there is an overpayment on the account, so HMRC takes the next month's payment by Direct Debit, and the overpayment is carried forward. It is very difficult to speak to HMRC/get the system corrected, so the easiest way to deal with this issue is to cancel the Direct Debit and make the next payment by bank transfer.

66. If the government decides to mandate payment by Direct Debit, HMRC will need to ensure that robust processes are in place to avoid problems like this – or to correct them immediately when they happen. Clearly no sanction should be applied to a business in this position for failing to pay by Direct Debit (see our response to Question 36).

67. A concern has also been raised with us about the scenario where the employment allowance has not been claimed at the start of the tax year. When it is claimed later in the year, would the system recognise the reduced amount due for the whole year?

68. It is unclear that HMRC's systems are robust enough to support the correct operation of Direct Debit payments by HMRC.

69. We have also been told that while some groups operate a single payroll across multiple legal entities, others maintain separate payrolls with different banking arrangements. Requiring PAYE liabilities to be collected by Direct Debit from only one nominated bank account could create unnecessary liquidity and cash-flow pressures, particularly where one entity is effectively funding payments on behalf of others.

Question 27: If you have used Direct Debit to make payments of PAYE to HMRC could you:

- **comment on any benefits of this method**
- **comment on any drawbacks of this method**
- **indicate whether this remains your chosen payment method and, if not, what prompted this change**

70. We have no comments on this question.

Question 28: If you currently pay PAYE by Direct Debit, to what extent does the later payment date influence your decision to use this method, compared to other factors?

71. We have no comments on this question.

Question 29: If it is made mandatory to make payment of PAYE by Direct Debit, what impact, if any, might this have on your business?

72. There are good reasons why many businesses do not choose to pay by Direct Debit (as outlined in our responses to Questions 12, 15 and 26).

73. If the government does decide to mandate payment by Direct Debit, there will need to be some exclusions, for example, for those making payments above £20m. We recommend that some businesses should also be offered the ability to opt out – see our response to Question 38 which discusses this in more detail.

74. If HMRC wants to encourage wider adoption of payment by Direct Debit (or if payment by this method is mandated), HMRC would need to take steps to address known problems and business concerns.

75. As a minimum, the problems with PAYE accounts outlined in our response to Question 26 need to be resolved.

76. If a requirement to pay by Direct Debit is introduced, HMRC should only take payments by Direct Debit for amounts shown in the RTI returns submitted by the taxpayer – not for any penalties or other amounts that may be showing on the PAYE account.

77. HMRC will also need to put in place a robust 'fast-track' process for dealing with any HMRC errors and correcting them rapidly. We discuss this further in our response to Question 38.

Question 30: Are you currently excepted from submitting electronic returns for PAYE?

78. We have no comments on this question.

Question 31: Please explain any barriers or challenges, if any, that you may face in making PAYE payments by Direct Debit?

79. See our responses to Questions 26 and 29.

Question 32: Are there any impacts on particular groups of taxpayers (such as disabled people; people of different ethnic groups, age, sex or gender, marital status, sexual orientation, religion; or people with or without dependents) that need to be addressed? How do you suggest we can overcome these?

80. We have no comments on this question.

Question 33: Have you ever made a payment of PAYE over £20million?

81. See our response to Question 34.

Question 34: If yes to 33, if you fluctuate above and below £20million please explain the typical range, frequency of fluctuation under and over £20million and why this varies?

82. We have received feedback that some large organisations do have variable monthly payroll amounts that would fluctuate above and below £20m; for example, this could happen where there are seasonal bonus payments.

83. This could also be the case for pension administrators, where drawdown payments vary depending on pensioner behaviour. For example, in the period around the end of the tax year pensioners may seek to take additional one-off drawdown payments. This could also happen in periods around fiscal events, where announcements (or speculation about possible changes) may prompt additional drawdown payments.

Question 35: If yes to 33, what is the lowest regular payment you have made in the past 3 years?

84. We have no comments on this question.

Question 36: What are your views on the use of penalties where VAT or PAYE is not paid by Direct Debit, including whether any penalty should apply on each occasion a payment is not made by Direct Debit, or if penalties should operate on a cumulative basis?

85. If the government decides to proceed with the proposal to mandate payment by Direct Debit, we do not support the imposition of penalties for failing to pay by Direct Debit.

86. As set out in our responses to earlier questions, there are good reasons why many businesses do not want to use (or would find it difficult to use) Direct Debits. Businesses should be able to choose the method of payment that works best for their circumstances. If a business is making payments on time, it should not matter to HMRC how it chooses to do this. Imposing penalties would not be reasonable or proportionate, particularly where the amount due has been paid in full and on time. There are already penalties (and interest) to deter late payment.

87. As noted in our response to Question 12, even well-managed businesses can experience genuine short term cash flow problems, for example following the insolvency of a major customer or a significant delayed payment. If a requirement to pay by Direct Debit is introduced, with penalties for failure to comply, HMRC should take account of this in considering when to impose penalties.

88. We assume that Time to Pay arrangements will continue to be available but in some cases it could be difficult for the business to set one up in time, leading to a failed Direct Debit. Again, this should be taken into account in considering any penalties.

89. If payment by Direct Debit is mandated, it is essential that some of the issues outlined above (that currently prevent businesses from using Direct Debit), are addressed and safeguards put in place. See our responses to Questions 17, 29 and 38.

Question 37: What challenges. if any, might arise from having different VAT or PAYE payment dates depending on the payment method used?

90. We assume this question relates to the suggestion in the consultation that extensions to payment deadlines for VAT and PAYE could be restricted to those paying by Direct Debit.

91. Clearly, if this approach is adopted, it would need to be communicated to all businesses. However, communications will be required anyway – either to encourage more businesses to pay by Direct Debit or to inform them that it will become mandatory to do so. Businesses which cannot pay by Direct Debit (but do pay electronically) should retain access to the extensions.

92. After an initial transition period, we envisage that there shouldn't be any ongoing challenges, as businesses which cease to be eligible for the extensions will adapt to the new rules.

Question 38: What other incentives or sanctions could be considered to encourage people to pay VAT and PAYE by Direct Debit.

93. As noted in our response to Question 36, we do not support the imposition of penalties for failing to pay by Direct Debit. Applying any sanctions would not be reasonable or proportionate where the amount due has been paid in full and on time.

94. A better approach would be to address the concerns that currently prevent many businesses from paying by Direct Debit, ensure that robust safeguards are in place and provide incentives to encourage more businesses to pay by Direct Debit. If the mandatory approach is taken forward, we recommend that some businesses should be able to opt out of paying by Direct Debit.

Ability to opt out of payment by Direct Debit

95. As set out in our responses to Questions 12, 15 and 29, there will be some businesses, particularly larger ones, and those in VAT groups, which will find it very difficult to pay by Direct Debit. If the government does decide to mandate payment by Direct Debit, there will need to be some exclusions, for example, for those making payments above £20m. We recommend that the government should also allow some businesses to opt out of paying by Direct Debit – and to pay by other (electronic) methods.

96. There could be conditions attached to opting out, for example, it could be restricted to businesses with a good payment record over a specified period. Businesses could be excluded if they are within the penalty regime for late payment.

Safeguards/addressing concerns

97. As a minimum, the problems outlined in our responses to Questions 12 and 26 with VAT and PAYE accounts need to be resolved, before businesses are required to pay by Direct Debit.

98. If a requirement to pay by Direct Debit is introduced, HMRC should only take payments by Direct Debit for amounts shown in the VAT or PAYE returns submitted by the taxpayer – not for any penalties or other amounts that may be showing on the VAT or PAYE accounts (see our responses to Questions 12 and Question 26). It isn't clear whether HMRC's systems are robust enough to ensure that it could do this.

99. HMRC should also put in place a robust 'fast-track' process for dealing with any HMRC errors and correcting them rapidly. Linked to this, HMRC will need to set out how it will deal with issues relating to the Direct Debit Guarantee – we assume that these may sometimes arise already, but if use of Direct Debit is mandated, volumes will increase significantly.

100. The Guarantee states that: "If an error is made in the payment of your Direct Debit, by the organisation or your bank or building society, you are entitled to a full and immediate refund of the amount paid from your bank or building society. If you receive a refund you are not entitled to, you must pay it back when the organisation asks you to."

101. The Guarantee also mentions that it "*only protects your Direct Debit payments. It doesn't cover you if you have a dispute with the biller."*

102. Where the business believes there is an error and invokes the Guarantee, HMRC will need to investigate the question of 'entitlement' quickly and efficiently.

Incentives and encouraging adoption of Direct Debit

103. Anecdotally, we have been told that the VAT Helpline may not always be very helpful when taxpayers ask about setting up Direct Debit payments. Considerable emphasis is apparently placed on the penalties that will apply if the Direct Debit is not set up at the right time, leading

people to decide to stick to payment by BACS, which they have often used for some time and which they can control.

104. A recent tribunal case W.Byers Ltd v Revenue and Customs Commissioners [2026] UKFTT 886 (TC) (which was decided in the taxpayer's favour) also indicates that HMRC may not be taking the most helpful approach (if it wants to encourage more businesses to use Direct Debit). HMRC wanted to impose late payment penalties because in its view the taxpayer did not set up the Direct Debit to pay its VAT early enough – it had apparently been "established on the same day as submission of the return." HMRC said that "according to their guidance, at least three working days' notice was required," even though the business received an onscreen automated confirmation stating that: "We will collect your payments automatically by Direct Debit."

105. We suggest that if HMRC wants to encourage greater take-up of Direct Debit (and certainly if payment by this route is mandated), it should recognise that there may be difficulties for businesses setting up a Direct Debit for the first time or reinstating one after a gap. HMRC communications must also be clear, and there could be more openness to accepting evidence that a 'reasonable excuse' exists, particularly where (as in the Byers' case) the taxpayer has arranged for the funds to be available.

106. We have been told about examples similar to the Byers' case where a Direct Debit was set up, but not in time, so businesses didn't make manual payments because the online account showed that a Direct Debit was in place (and instructed them not to pay by other methods). HMRC should ensure that communications are accurate.

107. We have also been told that (as appears to have happened in the Byers' case), it can take weeks for HMRC to let the business know that a Direct Debit has failed. Apart from setting the Direct Debit up too late, this could also happen where a Direct Debit has expired due to the length of time since any payment was taken. If a payment by Direct Debit fails for any reason, HMRC should notify the taxpayer immediately, so they have the opportunity to pay by another method quickly (and reinstate the Direct Debit, where relevant).

108. One incentive that could be introduced – for small businesses – would be to allow them to pay in instalments if they adopt payment by Direct Debit (without the need to follow the existing 'Time to Pay' application process). We understand that setting aside funds to make one big payment can be difficult for these businesses, so the ability to pay VAT over, say, two or three months, or PAYE weekly/fortnightly might make Direct Debit payments attractive and assist with financial management. HMRC itself recognises that spreading payments may be useful, in the proposals set out in the Timely Payments for income tax self assessment consultation to "smooth payments across the year."

109. This approach could help to prevent smaller businesses building up arrears. It could be restricted to smaller businesses, potentially by setting a turnover threshold for eligibility. It could also be withdrawn if payments were not made, to avoid some of the problems outlined in our response to Question 13.

110. Another potential incentive – but this would involve a cost to the Exchequer – would be to offer a 'discount' of a (small) percentage of the tax due, for payments by Direct Debit. Businesses incur costs collecting and administering VAT and PAYE on behalf of HMRC, so this might be attractive, but if businesses which already pay by Direct Debit are excluded, it would obviously be perceived as unfair. In view of the cost, it could be time-limited and restricted to smaller businesses (or a cap on the amount of the discount could be imposed).

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