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BASIS PERIOD REFORM

Response by Association of Taxation Technicians

1 Introduction

1.1 The Association of Taxation Technicians (ATT) is pleased to have the opportunity to respond to the HMRC consultation *Basis Period Reform* ('the Consultation')[1] and accompanying draft legislation[2] issued on 20 July 2021.

1.2 The primary charitable objective of the ATT is to promote education and the study of tax administration and practice. We place a strong emphasis on the practicalities of the tax system. Our work in this area draws heavily on the experience of our members who assist thousands of businesses and individuals to comply with their taxation obligations. This response is written with that background.

1.3 Overall, whilst we believe the proposed reforms present an opportunity for simplification, we are concerned about the proposed timetable and pace of change. We appreciate that the proposed changes will not affect the majority of unincorporated businesses that already have a 31 March or 5 April year end, but those who are affected face potentially significant additional administrative burdens and tax bills.

1.4 As set out in our response to question 10 below (see 3.14 to 3.19), many businesses are still struggling with the impacts of the COVID-19 pandemic, and the future outlook remains uncertain. In our view, introducing the proposed changes in 2022-23, followed immediately by the mandation of Making Tax Digital for Income Tax Self-Assessment ('MTD for ITSA') from April 2023, represents too much change in too short a timeframe. As a result we are concerned that taxpayers, agents and HMRC themselves will all struggle to cope.

1.5 We would therefore strongly recommend that the implementation of these changes be pushed back to allow for more consultation. Basis period reform should not proceed until tax year 2023/24 at the earliest, with MTD for ITSA also delayed to at least April 2024 allow time for that reform to bed in first.

1.6 We have set out our response to the specific questions posed by the call for evidence in Sections 2 to 4 below.

1.7 We would be pleased to discuss any aspect of this response further. Relevant contact details can be found in Section 5.

[1] https://www.gov.uk/government/consultations/basis-period-reform/basis-period-reform-consultation
[2] https://www.gov.uk/government/publications/income-tax-basis-period-reform

2 Chapter 3: Proposal: The tax year basis

Question 1: Do you think that the proposed 'tax year basis' for trading income is the best option for simplifying the basis period rules, and the best way to achieve simplicity and fairness between businesses? If not, do you think there is a better option?

2.1 We believe that, overall, the proposed tax year basis is the best option for simplifying the basis period rules. Whilst the proposal is not without its potential issues (as set out elsewhere in this response), it appears to deliver the best balance between simplicity and limiting adverse impacts for taxpayers.

2.2 We note that, in addition to the main proposal of moving to a tax year basis, the Consultation also proposes the following two alternative options:

- Mandating a 31 March or 5 April accounting date
- A corporation tax like approach with payment and return dates linked to the accounting period of the business.

We do not believe that either of these options are viable.

2.3 Whilst mandating an accounting date of 31 March or 5 April for all unincorporated businesses would apparently deliver simplification, this approach is too inflexible and does not take into account the commercial reasons why some businesses may choose to have a different year end.

2.4 For example, our members report that farmers commonly have a year-end other than 31 March or 5 April depending on their harvest / livestock sales times. We also understand that the accounting date of some large professional partnerships is dictated by the overseas networks of which they form part. Imposing a specific accounting date on these businesses would lead to significant difficulties for them and could, in some instances, provide an incentive to incorporate.

2.5 By contrast, whilst a corporation tax like approach would be very flexible, allowing businesses to choose their accounting period with filing and payment dates moving accordingly, this would not represent a real simplification. As noted in the Consultation, such a change would require significant adjustments to HMRC's systems, as well as those of taxpayers and agents. It would also not simplify reporting cycles under MTD for ITSA (something we understand to be one of the drivers behind basis period reform) and the differing deadlines could lead to confusion amongst taxpayers. Moving payment deadlines would also, presumably, have a cash flow impact for the Exchequer.

Question 2: Will the proposed tax year basis have an effect on how businesses choose their accounting date, and whether they choose 31 March or 5 April?

2.6 The proposed tax year basis is likely to result in some businesses choosing to move their accounting date to either 31 March or 5 April in order to avoid the need to apportion and estimate profits.

2.7 However, whether any one business decides to change its accounting date or not will depend on its individual facts and circumstances. For some businesses, it may not be possible, or desirable, to change to 31 March or 5 April.

2.8 As noted at 2.4 above, some businesses (such as farmers or professional partnerships) have different accounting dates for commercial reasons and would find it difficult to change these. In other industries, whilst a change may be possible, there would be wider implications of all businesses changing to the same accounting date. For example, pubs and restaurants normally use specialist stock takers to perform year-end stock takes

– if they all had the same accounting date, it could prove difficult to find an available stock taker. Hospitality businesses may also have chosen a year end other than 31 March to avoid both the risk of the year-end coinciding with Easter, and the 'two Easters' problem. This can arise when Easter is late in one year and early in another, with the result that the business could find that one year's accounts include the profits from two peak seasons rather than one, resulting in uneven profits (and thus tax bills).

2.9 Businesses may also prefer to have a different accounting date where it helps them to make informed financial decisions. For example, for pensions purposes, one driver for a different year end is to allow the taxpayer time to calculate the level of contribution which can be made in a tax year. A non-March accounting date allows far more time to draw up accounts and plan and arrange accurate pension contributions. By contrast, a 31 March accounting date would require taxpayers to make an estimate of how much they can contribute. As a result, some individuals may not be able to maximise their pension contributions in a year, or will make over-estimates of what they can put in, which will create additional administration burdens. One option might be to consider whether pension contributions could be carried back, once profits are known, but we appreciate that would be a significant change.

Question 3: For businesses with a non-tax year accounting date, what would be the cost of the additional administrative burden of apportioning profits into tax years? Are there any simpler alternative approaches to apportionment?

2.10 The additional administrative burdens and costs arising from the requirement to apportion profits will depend upon exactly how this exercise is to be carried out.

2.11 We assume that the approach would be to calculate the taxable profit or loss (for avoidance of doubt, *after* consideration of capital allowances) on an accounting period by accounting period basis (as is currently the case), before then splitting this between the relevant tax years on a time basis. This would be the most straightforward approach, and would be far preferable to any more complex alternatives such as requiring individual items of income and expense to be allocated between tax years.

2.12 If our assumption is correct, then we would anticipate apportionment to not be overly problematic in practice once the relevant sets of accounts have been prepared. It should be an exercise which software should be able to handle (in a similar way to how corporation tax software currently apportions profits of an accounting period between tax years). Instead, we believe the greater administrative burden will arise where there is a requirement to estimate profits and file amended returns (as discussed in our response to questions 4a and 4b below).

2.13 Consideration will, though, need to be given as to exactly *what* information is reported in the self-assessment return each year when apportionment applies – i.e. what the tax return will look like when apportionment is in play. (This will also have an impact on the burden for correcting estimates as discussed below.)

2.14 By way of example, under the current system, a sole trader with a September year end generally makes a report each year of the details of the single set of accounts to the relevant year end, followed by any necessary tax adjustments (for example for opening years) reported as a single figure on the self-employment pages of the return. So for 2019/20, an individual with an ongoing business would report details of their income and expenditure to 30 September 2019 on the self-employment pages. Following the change to a tax year basis, the taxable profits for the 2023/24 tax year, say, will be based on the 30 September 2023 and 30 September 2024 accounts. What is HMRC expecting to be reported for 2023/24?

One option would be for the individual to continue to report the details of 30 September 2023 accounts in full followed by:

- adjustment to show the apportionment to six months of the reported figures
- a further, single, figure reporting the profits relating to the 30 September 2024 accounts which need to be added. This figure will initially be an estimate in many cases, with the final figure updated later.

Alternatively, is the intention that full information will be needed for both accounting periods which are being apportioned to make the 2023/24 profit figure in order to give HMRC a full picture of the year within the return? I.e. Would details of both 30 September 2023 and estimates of figures to 30 September 2024 accounts be required?

We suggest that for simplicity that the current pattern of reporting the accounts ending in the tax year in full, followed by single figure adjustments as necessary should be retained. Whichever approach is taken, detailed guidance for both taxpayers and agents will be needed.

Question 4a: Businesses with accounting dates later in the tax year will have to estimate profits for a proportion of the tax year, before accounts are prepared. For which accounting dates do you think this would be necessary? Do you expect that businesses that have accounting dates earlier in the tax year than 30 September will have to estimate profits? If so, which types of business would be affected?

2.15 Our members report that any accounting date from 31 July onwards could lead to a requirement to estimate profits. The Consultation's suggestion of 30 September only allows for a period of six months for accounts to be produced, and spans the summer holiday months and the usual busy season for ITSA returns. Based on their experience, our members feel this would be insufficient. We would also note that private limited companies have nine months to produce their (albeit more complex) statutory accounts for Companies House.

2.16 Members also report that the following types of businesses may be particularly affected by the requirement to estimate profits:

- Farmers – often busy during the summer months or waiting on crops to mature may find it commercially difficult to change their accounting date.
- Partnerships – any delay in preparing partnership accounts would affect all partners.
- Doctors (in particular GPs)– often partnerships and generally have large amounts of information to gather. They also need to take into account the interaction with superannuation certificates which determine pensionable profits based on taxable profits.

We have made some more detailed notes on farming and GPs below (see 4.1 to 4.2). Of these points, the key element where additional work will be needed is in respect of averaging where clarity is needed to ensure this is approached consistently.

2.17 To reduce the number of businesses required to make estimates, consideration could be given to introducing a later ITSA return filing deadline for those with an accounting date later in the year. Any possible incentive to pick a later accounting date in order to benefit from this would be at least partially countered by the additional burdens arising from the need to estimate profits. The potential Exchequer impact of such a move could also be avoided (or at least significantly reduced) by requiring those businesses to make an additional payment on account of their liability for the tax year by the normal filing deadline of 31 January. It would essentially be the filing rather than the payment date which was changed.

Question 4b: Will estimation be a significant burden for those businesses affected, and what will the cost be? Are there any simpler alternative methods of estimating profit or finalising estimates, which could mitigate any extra administrative burden?

2.18 Under the proposed tax year basis, businesses who choose to retain their non-March year end will be forced to make estimates – and then correct them – on an annual basis. Currently such businesses only make an estimate in opening years, before settling into a pattern of filing returns based on a single set of finalised accounts. Any burdens which arise from the change will be enduring. In the interests of clarity, we will consider separately the potential burdens arising from estimating profits and then subsequently finalising that estimate.

Estimating profits

2.19 We anticipate that the requirement to estimate profits will represent a significant burden for affected businesses.

2.20 Similar to apportionment, the exact level of this burden will depend upon how estimation is expected to be carried out in practice. In particular, the level of accuracy expected of estimates, and the amount of information that the business needs to report to support that estimate, will affect how challenging this is. The size of the business will also increase the complexity of estimations.

2.21 In general, we think that businesses should be allowed to make estimates in the way they best see fit.

2.22 The approach to estimation is likely to involve consideration of the outcome of previous years returns, the 'known' part of the year to date, any budgets or forecasts for those businesses that do prepare these in detail, and a discussion with the business owner as to their expectations of future performance, any known costs or capital expenditure that are out of the ordinary and so on. For more substantial businesses and partnerships, this could amount to a number of hours of chargeable time by an agent, including time discussing the estimate with the client, on an annual basis.

2.23 For smaller and/or unrepresented businesses the work of estimation should be less and in some cases something more mechanical such as a simple estimation by estimating turnover for the appropriate period and then applying a specific percentage (based on either the specific business or particular industry) to arrive at the taxable profits may be appropriate.

2.24 It is also important to consider at this stage what information HMRC would like to see in respect of estimates and when that would be provided. The burden would be very high indeed if full tax calculations including a line by line break down of income and expenditure were required for the estimated period. We assume therefore that HMRC will not require any additional information beyond the single, estimated profit figure which is needed to establish the taxable profits for the tax year. This would be in line with the current requirements for opening years rules (see for example box 68 on the Self-employment (full) pages on the SA103(F) in which a single figure is used to adjust the detailed report from the relevant accounting period.[3])

2.25 We note that the Consultation proposes the following alternatives to estimation:

- Basing estimates on MTD quarterly updates
- Extrapolation of profits from 'known' part of tax year

We do not believe either of these are viable.

[3] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/975346/sa103f-2021.pdf

2.26 As noted in our response to the recent HMRC call for evidence on Timely Payment[4], we do not believe it is feasible to use MTD quarterly updates as a basis for calculating tax liability. These updates are not required to include tax or accounting adjustments and, given the complexity of the ITSA rules, it is highly unlikely that they will give a reliable indication of final tax liability.

2.27 Extrapolation of profits from the 'known' part of the tax year is also unlikely to be appropriate in practice. In particular, it would not be suitable for seasonal businesses or those with an accounting date early in the tax year when the 'known' part of any tax year could be very small.

2.28 Whichever approach is taken; we would strongly recommend that no penalties apply where a business has made a reasonable estimate which later turns out to be too low. At most, such underpayments should attract an interest charge only, and we would also expect HMRC to pay interest on overpayments arising from an excessive estimate.

Finalising estimates

2.29 The proposed requirement to file an amended return to finalise an estimate will result in extra administrative burdens and advisers' fees for those taxpayers affected.

2.30 As noted above at 2.24, consideration also needs to be given to the potentially significant changes to the self-assessment return, systems and processes to facilitate the correction of estimates. We presume the simplest approach will be to amend the previous year's return for the estimated figure, replacing it with the actual apportioned figure from the following years' accounts - which will then be reported as part of the following year's tax return.

2.31 We are though concerned as to what effect filing frequent amendments could have on the perceived 'risk' of a business in HMRC's eyes, and whether an amendment to finalise an estimate would result in the enquiry window for the return in question being extended.

2.32 One alternative could be to introduce a standalone process for finalising estimates. This could be along the lines of a streamlined version of the current amendment process, but dedicated to this purpose only. Decoupling finalisation of estimates from the standard amendment processes in this way would address concerns about enquiry windows, risk profiling etc. Alternatively, these could also be addressed by making it possible for taxpayers to indicate (for example by ticking a specific box) that an amendment solely arises due to correction of an estimate. We would be pleased to discuss the practicalities of this suggestion.

Question 5: Would the proposed equivalence of 31 March to 5 April help businesses that would have to make apportionments to work out their profit or loss under the tax year basis? Would extending this equivalence to property income help property businesses, which would otherwise have to apportion profit or loss each year? Are there any problems with this equivalence proposal?

2.33 We believe the proposed equivalence to be a sensible suggestion, and would welcome its extension to property businesses.

2.34 We note that this proposed equivalence would also limit the impact if the tax year end were to be changed to 31 March following the outcome of the current Office of Tax Simplification review[5]. It would not, however, address the issues which could arise if the outcome of that review was to change the tax year end to 31 December.

[4] https://www.att.org.uk/sites/default/files/210712%20Timely%20payment%20-%20ATT%20response.pdf
[5] https://www.gov.uk/government/publications/ots-to-explore-potential-for-moving-the-end-of-the-tax-year

2.35 One area which would require further consideration is how this equivalence will interact with the operation of the Construction Industry Scheme (CIS). CIS reporting currently runs to 5 April each year – how could this be reconciled for a trader who draws up accounts to the 31 March?

Question 6: Are there any specific issues, costs, or benefits to the tax year basis for partners in trading partnerships?

2.36 As noted at 2.4 above, large professional partnerships may have an accounting date other than 31 March or 5 April due to being part of an international network with aligned reporting dates. These partnerships are unlikely to be able to change their accounting date, and will therefore have to undertake apportionment and potentially estimation as well.

2.37 From a practical perspective, the change to a tax year basis will make matters more difficult where not all the partners in a partnership are dealt with by the same agent who will need to agree who has responsibility for preparing estimates.

Question 7: Are there any other issues and interactions to consider for the tax year basis, or the transition, in the areas of tax outlined in paragraph 3.33?

2.38 Paragraph 3.33 of the Consultation lists a number of issues and potential interactions. A key point for some of these, such as the High Income Child Benefit Charge (HICBC) and student finance repayments, is what measure of profits will be used in the transitional year 2022/23 and subsequent years? This consideration will apply equally to issues not identified in that list, such as the withdrawal of the personal allowance for higher earners. Our recommendation is that the impact of transitional and spreading adjustments be ignored for these purposes. It would not be a desirable outcome, for example, for more taxpayers to be brought within the remit of the HICBC just for the transitional year, or due to the inclusion of a spreading adjustment.

2.39 Another of the areas identified in paragraph 3.33 is capital allowances. We understand that these reforms should not result in a decoupling of capital allowances (or charges) from the calculation of profits for the period of account in which the expenditure was incurred. That is, capital allowances would be calculated for the period of account (as usual), with the overall profit / loss after their inclusion then being apportioned as required to the tax year in question. This approach seems sensible. We would definitely not support any alternative system under which businesses were required to calculate capital allowances by reference to the acquisitions and disposals actually occurring in the particular tax year. This would create significant additional work. Practitioners are already familiar with the principle of calculating profits for opening year rules after deduction of any estimated or known capital allowances and it would be helpful if this practice could continue.

2.40 Averaging of fluctuating profits is also identified in paragraph 3.33, and we believe that this may be a particular problem for farmers and for creative artists. As noted at 2.4 above, farmers may have accounting dates other than 31 March or 5 April for commercial reasons. There are a few areas of concern around averaging which we have picked up in more detail in 4.1 and 4.2 below.

3 Chapter 4: Implementation and transition

Question 8a: Does the proposed method of transitioning to the tax year basis using a long basis period combined with allowing all unused overlap relief achieve the best balance between simplicity and fairness? If not, is there a better option for transition?

3.1 We believe that the proposed transition method appears sensible.

3.2 However, one area of concern is the impact on taxpayers who do not have a record of their original overlap. This may be particularly common amongst older businesses, as well as those who have changed agent since commencement. This issue is acknowledged in the Executive Summary to the Consultation, which states that "It is common for businesses to lose track of their overlap relief, which may date from more than 20 years ago".

3.3 To address this, we would ask that HMRC put in place a system provide figures (and where necessary, calculate) overlap relief to affected taxpayers. This would be of significant benefit not just to those taxpayers who could otherwise miss out on relief due, but also to HMRC in terms of allowing verification of amounts included in returns and ensuring that excessive relief is not claimed.

3.4 Ideally, from the perspective of agents, it would be helpful if this information could be supplied via an API which software developers could incorporate into their systems. Agents who already have the relevant information can then check for differences/discrepancies to what information HMRC holds. Alternatively, it would be helpful if the overlap information could be suppled through either the individuals' Personal or Business Tax Account (with a suitable alternative for the digitally excluded). While we appreciate there would be costs to this, it might usefully incentivise take up and engagement of taxpayers with their Personal/Business Tax Accounts. Whatever approach is taken, it will be important that overlap information is available equally to both taxpayers and their agents.

Question 8b: Are there any other specific circumstances on transition to the tax year basis that would require additional rules?

3.5 One area of concern is whether the ability to spread excess profits will be available to those who have changed accounting date in anticipation of this reform.

3.6 The draft legislation currently states at paragraph 36 of Schedule 1 that a spreading adjustment can only be made where there is a 'transition period'. This is defined as being the period (if any) beginning immediately after the end of the basis period for the tax year 2022/23 and ending with 5 April 2023. Our reading of this is that, where a business changes its accounting date prior to 5 April 2023, they will not have a 'transition period' and therefore will not be able to spread any excess profits arising.

3.7 We understand from discussions with HMRC that this consequence is not intentional, and that there is no wish for those who (sensibly) change their accounting period in 2022/23 to be disadvantaged. To ensure this is not the case, the definition of 'transition period' needs to be adjusted accordingly.

3.8 We would also recommend that consideration be given to allowing those who change accounting date in the current tax year 2021/22 to spread any excess profits which could arise. Changing in this way will simplify matters for the business in question (in removing the need to estimate / apportion profits) and it would seem counter-intuitive to remove the incentive to do so, or penalise those who may have done so already.

Question 9a: Would the proposals for spreading excess profit mitigate the impact of transition without affecting the simplification of moving to the tax year basis? If not, are there any other ways of mitigating the transition impact that you would suggest?

3.9 We believe that the proposals for spreading excess profits are a sensible approach to mitigating the transition to a tax year basis.

3.10 We note that the draft legislation indicates at paragraph 38 of Schedule 1 that ceasing to trade during the spreading period will result in the balance of any transitional period profits being brought into account in the tax year of cessation. Whilst we believe this approach is sensible, it could catch some unsuspecting businesses unawares, and we would therefore recommend that this is highlighted in all relevant guidance.

Question 9b: Would the proposal to spread excess transitional profits over five years be enough to resolve the cash flow impacts of the proposed reform? Are there any situations which would need additional rules or anti-avoidance provisions?

3.11 On balance, we believe that the current proposal to spread excess transitional profits over five years is sensible, and welcome the option provided for in paragraph 39 of Schedule 1 of the draft legislation to elect to spread over a shorter period of time.

3.12 However, there may be cases where a longer period of spreading would be helpful due to the amount of extra tax at stake. This could be the case, for example, where the current accounting date causes a large amount of extra profits to be taxed in the transitional period (a 30 April accounting date could result in 23 months of profit being brought into account in 2022/23) or there is a lack of overlap profits due to losses or low profits in the early years of trade. In such cases, consideration should be given to allowing those affected to apply for a longer spreading period of up to ten years, subject to HMRC approval. Alternatively, a threshold (whether in monetary or percentage terms) could be introduced, such that where excess profits exceed that level a longer spreading period applies.

3.13 Looking at the draft legislation on spreading, we have one minor comment. Para 39(3) of Schedule 1 states that *"The election must specify the amount to be treated as arising in the tax year…."*. For consistency with both 39(1) and 39(4), it might be helpful if this was stipulated as the "additional amount".

Question 10: Are there any other impacts, benefits, or costs in the core policy, transition, or mitigation proposals that we have not considered above?

3.14 As noted in our introduction, we are concerned about the timescale for this change, and the interaction with the proposed mandation of MTD for ITSA in April 2023. Together, basis period reform and MTD for ITSA represent a large amount of change for taxpayers, agents and HMRC in a very short period, and at a time when many will still be recovering from the impact of the COVID-19 pandemic. Recently, the ATT, along with other professional bodies, wrote to the Financial Secretary to the Treasury[6] to outline our concerns over the proposed timetable for these changes and the potential for them to undermine trust in the tax system.

3.15 Even without taking into account the current proposals for basis period reform, preparations for MTD for ITSA are not as advanced as we would like to see them given the relatively short period of time which remains until mandation. The actual requirements for quarterly updates have not yet been confirmed, detailed legislation is not available, the software market is under-developed and the pilot remains severely limited in scope. As a result, agents and taxpayers are not yet able to start meaningful preparations for mandation, and introducing these basis period reforms in 2022/23 will act to further reduce the time available to prepare.

3.16 A further implication of basis period reform is that all MTD for ITSA quarterly updates will be prepared to cover the same period and have the same filing deadlines. Whilst this does appear to be a simplification, it will result in a large number of filing deadlines falling in the same short period of time. For example, January each year will see agents finalising self-assessment tax returns (deadline 31 January), handling MTD quarterly updates

6 https://www.att.org.uk/sites/default/files/16%2008%2021%20Joint%20professional%20bodies%20letter%20re%20basis%20period%20reform%20and%20MTD....pdf

for the quarter ended 31 December (deadline 5 February) and completing VAT returns for those clients on stagger 1 (deadline 7 February). Our members are concerned as to the impact this 'bunching' will have on their workloads, and the ability of HMRC's systems and helplines to cope with all businesses reporting, and potentially needing assistance, at the same time. These concerns will potentially be exacerbated if more businesses, understandably, choose to change their VAT stagger to align with their MTD for ITSA quarterly update cycle.

3.17 We are also concerned about the pressure that HMRC's already strained resources will be put under if basis period reform and MTD for ITSA are introduced in the timetable proposed. Our members frequently report problems in getting hold of HMRC via telephone or webchat, as well as severe delays to processing of post. Basis period reform and MTD for ITSA will lead to an increase in taxpayers and agents contacting HMRC for support and assistance, something which will only exacerbate current service problems.

3.18 Finally, we would query the interaction of these reforms with the OTS work on the tax year end. As noted at 2.34 above, if this were to result in the tax year end changing to 31 March there would be minimal impact on these proposals. However, if a more radical change to 31 December were favoured, this would be a marked shift, and we would not want to see another re-alignment of the basis period rules required in a few years' time.

3.19 Overall, we would therefore strongly recommend a delay in the roll-out of both these proposals and MTD for ITSA. This would allow for a proper period of consultation, avoiding the potential pitfalls which could otherwise arise from a rush to reform. It would also allow more time for the recommendations of the OTS to be considered, and for businesses, agents and HMRC to get to grips with the practical requirements of both basis period reform and MTD.

4 Chapter 5: Assessment of impacts

Question 11: : Please tell us if you think there are any other specific impacts on other groups or businesses that we have not considered above.

4.1 In response to this question we would like to go into more detail on some areas which have been raised by our members regarding:

- Farmers
- Creative artists
- Doctors (particularly GP practices)
- Lloyds Underwriters

Farmers and GP practices are discussed in more detail in Appendix 1.

4.2 For farmers and creative artists, serious consideration is required in respect of how averaging is intended to work. There are three elements to consider:

1) Will averaging be permitted in the transitional year when establishing the 'usual' profits under existing basis period rules?
2) Will future averaging be allowed to include the transitional year?
3) Should any such averaging be before or after the excess profits adjustment?

Consideration may also need to be given to time limits for amending averaging claims.

We have set out more detail on these issues in Appendix 2.

4.3 For Lloyds Underwriters, we assume that any remaining Names within income tax will be allowed to continue under the specific rules which are already in existence on the grounds it would not be possible to report on a current year basis.

5 Contact details

5.1 We would be pleased to join in any discussion relating to the Consultation. Should you wish to discuss any aspect of this response, please contact our relevant Technical Officer, Emma Rawson on 07773 087111 or erawson@att.org.uk.

The Association of Taxation Technicians

6 Note

6.1 The Association is a charity and the leading professional body for those providing UK tax compliance services. Our primary charitable objective is to promote education and the study of tax administration and practice. One of our key aims is to provide an appropriate qualification for individuals who undertake tax compliance work. Drawing on our members' practical experience and knowledge, we contribute to consultations on the development of the UK tax system and seek to ensure that, for the general public, it is workable and as fair as possible.

Our members are qualified by examination and practical experience. They commit to the highest standards of professional conduct and ensure that their tax knowledge is constantly kept up to date. Members may be found in private practice, commerce and industry, government and academia.

The Association has more than 9,000 members and Fellows together with over 6,000 students. Members and Fellows use the practising title of 'Taxation Technician' or 'Taxation Technician (Fellow)' and the designatory letters 'ATT' and 'ATT (Fellow)' respectively.

Appendix 1: Impact on farmers and GP practices

Farmers

In respect of farmers – and their advisers - there are two potential areas of impact to be aware of. These are the difficulties of adopting a March year end which is not a natural point in the farming cycle to terminate accounts, and the implications for averaging – which also affects creative artists. We expect small and medium-sized farmers and their advisers will adopt a pragmatic approach to the former, although it will mean more accounts – and thus tax bills - based on the estimated value of growing crops according to HS232. The averaging point will require legislation (supported by detailed guidance) to set out how averaging claims over the transitional period are to work.

We noted at 2.4 that there are a number of commercial reasons why some farmers may not wish to adopt a March year end. By way of more specific examples:

- Arable farmers/market gardeners – for many such farmers and growers, the choice of year is dictated by when crops have been harvested and either sold, or quantities known which can be valued. For example, winter wheat is drilled (sown) in around October to November and spring wheat in early March. Both are harvested in July-August. A year end of 31 March therefore means having to calculate the value of growing crops according to the methods set out in HS232[7] which means that tax is then based on a valuation which could be seriously affected by subsequent weather or market shifts. Businesses in this position may wish to retain a September year end to ensure their accounts reflect actual outcomes from a given growing season.
- Sheep farmers – although some farmers start to lamb indoors as early as December or January, for many sheep farmers, the peak lambing season is March/April. A 31 March year end is therefore undesirable because of the workload during that period (lambing is a 24hr operation).
- Dairy - calving is usually staggered over the year, while for pigs and poultry the cycles are short enough that a March year end should be less likely to be disruptive.

GP practices

A number of members have highlighted concerns about the specific impact of these proposals on GP practices. These are operated as partnerships which have contracts to provide services to the NHS. Since the NHS operates to a 31 March year end many practices have adopted this as their year-end and ultimately, a 31 March year end is likely to be a more sensible option for many GP practices. However, we think it is important to note that there will be a transitional impact on GPs in practices which do not already have a March year end. Of these, the primary concern expressed to us is in respect of the impact on GP superannuation and the pensions annual allowance.

GP partners are allowed to be part of the NHS pension scheme and each year it is necessary to prepare a superannuation certificate to calculate their pensionable pay and determine what their contributions should be. The starting point for the computation of pensionable pay is the taxable profits of the relevant tax year.

Assuming NHS Pensions decide to adopt the tax year basis for taxable profits (and we presume also make provision for spreading elections to avoid spikes in pensionable pay and contributions), the concern is that as overlap profits are expected to be low compared to current profits, this will result in an increase in pensionable pay over five years. While this may bring benefits in the longer term, some GPs, particularly older ones who have been partners for many years (and who are more likely to have low overlap profits) may find the changes are sufficient to bring them within the scope of annual allowance charges.

[7] https://www.gov.uk/government/publications/farm-stock-valuation-hs232-self-assessment-helpsheet/hs232-farm-stock-valuation-2017

A practice specialising in GP practices have reported to us that despite the recent changes to the tapering limit they are still seeing a significant number of GPs suffering annual allowance charges (due to not having unused allowances available as a result of the historic tapering rules) and hikes in pensionable pay generally result in large growth in projected pensions. They have expressed concerns that the impact on pensions could result in some older GPs deciding to draw their pensions and leave the profession. The firm also reports seeing doctors coming in and out of the NHS Pension scheme to reduce annual allowance tax charges and these changes are likely to make these calculations even more complicated.

One approach to minimise the effect in the transitional period might be to allow NHS members to choose how much income they pension in the transitional year and for four years afterwards.

Other specific concerns raised with us include:

- Practice incomes have been difficult to predict during the pandemic, making estimates challenging. It is unclear how long this will continue to have an impact on practice income and expenses.
- Unlike small, family-based partnerships, GP practices can be large with the partnership involving a number of unrelated individuals, some of whom may also have external income which is brought into practice accounts and then prior shared to them in what can be complex profit sharing agreements – all of which will mean the work of producing estimates of future profits and amending returns for non-March year ends will be more burdensome.
- Amendments to taxable profits to finalise estimates will also mean additional work amending superannuation certificates. Again this will incur additional administration time and costs for the practice.

GPs tend to plan their retirement a long time in advance as succession planning can be challenging, with younger doctors more reluctant to take on partnership responsibilities. Advance planning is particularly advised for those in non-March year end practices as getting the timing wrong can result in additional tax and annual allowance liabilities. The short timescale for the introduction of these measures could adversely affect those who are planning to retire in the next few years.

Appendix 2: Farmers averaging worked examples

To illustrate the issues around averaging, we thought it would be helpful to use an example. For simplicity we are only looking at two-year averaging (which also applies for creative artists) and not the extended five year averaging that farmers are permitted.

Farmer Giles has a year end of 30 September, has been trading for some years and has overlap profits of £5,000. His profits are as follows:

- 30 September 2021 - £10,000
- 30 September 2022 - £20,000
- 30 September 2023 - £40,000
- 30 September 2024 - £15,000

Note that in each year his accounts may well be only finalised after 31 January, leading to the use of estimates and subsequent reworking and finalisation

Looking at each tax year in turn.

2021/22

In 2021/22 he will be taxed on the profits for the year ended 30 September 2021 **- £10,000**. For the purposes of this example we assume he does not opt to average with the previous year.

2022/23

In 2022/23, which is the transition year, he would absent these reforms have been taxed on profits in the year ended 30 September 2022 - £20,000. However, since averaging is permitted as £10,000 is less than 75% of £20,000, we assume he would have opted to average. The profits for 2021/22 will be reassessed as if he had taxable profits of £15,000 (being the profits of both averaged years added together and divided by two) and the assessable profits of 2022/23 will be £15,000 also.

Under the new rules however, in 2022/23 Farmer Giles will be assessed on the standard component – defined by the current year basis - plus the transition component, less overlap relief.

Profits under 2022/23 transitional rules (before spreading of excess profits) will be:

Year ended 30 September 2022	20,000	
Plus: 6months of year ended 30 September 2023	20,000	(NB This will likely be an estimate when first prepared)
Less: Overlap relief	(5,000)	
Taxable profit for 2022/23	**35,000**	

Question 1: The "excess profits" for spreading is the difference between the profits under the transitional rules and the 'usual' profits. Are the usual profits the figure before or after averaging with 2021/22? In this example the excess profits could be either £35,000 - £20,000 = £15,000 (being the difference between the taxable profits in the transition year and just the accounts ending 30 September 2022), or £35,000 - £15,000 = £20,000 - being what Farmer Giles's profits *after* averaging would be.

In our view, the excess profits for spreading should be calculated in relation to the profits for 2022/23 *after* any relevant averaging claim relating to prior years. I.e. When determining their 'normal' or 'usual' profits for calculating excess profits, farmers should be able to apply averaging to the previous year(s) that they would otherwise have done in the absence of any changes. (NB Averaging for farmers can be over 2 or 5 years – this doesn't change the principle).

On this basis, Farmer Giles's taxable profits for 2022/23 in the transition year would be £35,000 less the 'excess' of £20,000 plus 1/5th of the excess £4,000 = **£19,000**.

Questions 2 & 3: Can the figure ultimately determined as the profits of the transitional year then be averaged with the previous (or following) years? If so, should this be before or after the spreading adjustment?

We think since the figure ultimately arrived at for 2022/23 (excluding the spreading adjustment) should represent 12 months of profits, it should be permissible to average with previous years. (This will be relevant for the provisions of the five year averaging more so than two year averaging.) Averaging should be done *before* the spreading adjustment is added in to ensure that the figures being averaged are comparable and to ensure farmers are not perceived to be getting an advantage over other trades.

As a further complication, without the change of rules to a tax year basis, when considering 2023/24, Farmer Giles would potentially be able to average 2022/23 with 2023/24. So in the absence of a rule change, in 2023/24 he would take his profits from the year ended 30 September 2023 of £40,000 and average them with the £15,000 profits assessed as taxable in 2022/23 given a new taxable profits figure of £27,500 for each year. If this second round of averaging was allowed to be used when determining the 'usual' profits in 2022/23, it would have a knock on effect on the excess profits figure for 2022/23. **We suggest that in order to achieve certainty and avoid further complexity, when determining the 'usual' profits for 2022/23, averaging is only allowed with previous years and not future years.**

2023/24

We are now in the new rules, so Farmer Giles' profits are calculated by apportionment (we are using months for simplicity, a proper calculation would use days)

Six months of the year ended 30 September 2023	£20,000 (being 40,000 x 6/12)
Six months of the year ended 30 September 2024	£7,500 (being 15,000 x6/12)
Total	£27,500
Plus 1/5th of the excess profits from the transition year	£4,000
Taxable profits (pre averaging)	£31,500

Again, the question arises, can the 2023/24 be averaged with 2022/23 and, if so, before or after the spreading adjustment? We think that averaging should be permitted, but with the figure of £27,500 – i.e. before the spreading adjustment.

Legislation will be needed to prescribe the steps in order that must be taken for the avoidance of confusion by practitioners.

From a practical perspective, it may also be helpful to allow more time than the current one year from the 31 January following the tax year allowed under s225 ITTIOA 2005.