Finance Bill 2021-22

Representation from the Association of Taxation Technicians (ATT)

Clause 7 and Schedule 1: Abolition of basis periods

Executive Summary

Whilst this reform may remove some of the complexities of the current basis periods regime, especially for new businesses, it will bring increased complexity, administrative burdens and costs for the minority of businesses who do not draw their accounts up in line with the tax year. HMRC need to focus efforts on limiting the practical impact on these businesses as much as possible.

Whilst we welcome the government's decision to defer this reform until 2023/24, we remain concerned that it will take effect just a year before the introduction of Making Tax Digital for Income Tax Self-Assessment. The introduction of two large reforms to income tax calculation and reporting in the space of two years will place a significant burden on all involved. We have serious concerns as to whether taxpayers, agents and HMRC will be able to cope.

HMRC must be adequately resourced to support taxpayers and their agents throughout this time. HMRC have recently acknowledged a six-month backlog of work which has resulted from the heavy demands placed on the department as a result of Brexit and operating the various Covid schemes. These additional changes will add to the burdens of both taxpayers and HMRC.

Background

1.1. Under the current basis period rules, the income tax paid by sole traders and trading partnerships in any tax year is based on the profits earned in the accounting period ending in that tax year. The accounting period end chosen by these businesses therefore directly affects which profits are taxed in each tax year.

1.2. Clause 7 and Schedule 1 abolish these basis period rules such that, from 6 April 2024, the tax payable by these businesses will instead be based on the profits which they actually earn in the tax year.

1.3. The majority of sole traders and partnerships[1] already draw up their accounts to align with the tax year, and therefore won't be affected by this change. However, those businesses that don't draw up their accounts in line with the tax year will face an increase in their tax bills over a period of up to five years, as well as ongoing increases in administrative burdens and costs.

1.4. This reform was the subject of a short HMRC consultation over the summer of 2021[2]. In our response to that consultation[3], we called for it to be delayed from its originally planned introduction date of April 2023 to allow further time for consultation. We therefore welcomed the announcement of such a delay by the Government on 23 September 2021. However, as set out in section 2 below, we consider that it is vital that HMRC make use of

[1] 93% of sole traders and 67% of partnerships according to the HMRC consultation published on 20 July 2021
[2] https://www.gov.uk/government/consultations/basis-period-reform/basis-period-reform-consultation
[3] https://www.att.org.uk/technical/submissions/basis-period-reform

this extra time to further explore how the practical and financial impacts on affected businesses can be limited.

1.5. Our response to HMRC's consultation also highlighted concerns about how any extra profits arising on the changeover to the new regime could affect existing allowances and charges, such as the tapering of the personal allowance for high earners, and the High Income Child Benefit Charge. We therefore welcome that the legislation has been revised to reduce the impact on these allowances and benefits.

2. Complexity and HMRC resources

2.1. This reform is being introduced by the Government as a supposed simplification measure. Whilst it may simplify the existing rules for some – especially new businesses – this needs to be weighed against the significantly increased complexity, administrative burdens and costs which will arise for the minority of existing businesses who do not draw their accounts up in line with the tax year.

2.2. Depending on the accounting date they use, some of these businesses will not have final accounts ready by the time they come to prepare their tax returns. As a result, they will be required to estimate a portion of their taxable profits each year, and then correct their position once their final results are known. HMRC's efforts should be directed towards making this process as streamlined and simple to apply as possible, to limit the ongoing time burdens and costs involved.

2.3. Whilst some businesses may be able to change their accounting date to align with the tax year, and therefore remove some of these burdens and costs, this may not be commercially possible or desirable for some. For example, farmers often choose a year-end other than the tax year, as a spring year end would fall at a bad time for lambing, crop valuation etc. Other industries likely to be affected include retail and hospitality (who may prefer a year-end away from the busy Easter period) and large professional partnerships who are part of international networks.

2.4. We understand from oral evidence given by HMRC to the House of Lords Economic Affairs Finance Bill Sub-Committee[4] that around 20% of the businesses that will face these additional burdens are 'unrepresented', meaning they do not have a tax agent and instead handle their tax affairs themselves. It will be important for HMRC to undertake a detailed information campaign to make these unrepresented taxpayers aware of the changes, as well as ensuring they have the resources on hand to support them through it.

3. Timetable and pace of change

3.1. As noted at 1.4 above, we were very concerned over the previously proposed timetable for this reform, so were pleased to see the announcement on 23 September 2021 that it would be delayed by one year. However, we remain concerned over the interaction of this reform with the introduction of Making Tax Digital for Income Tax Self-Assessment (MTD for ITSA) from April 2024.

3.2. MTD for ITSA is due to be introduced for unincorporated businesses with income above £10,000 a year from April 2024. This will represent a fundamental change in how many businesses manage their tax affairs and interact with HMRC. In particular, those businesses

[4] https://committees.parliament.uk/oralevidence/2981/pdf/

in scope will be required to use specific compatible software to keep their records and file quarterly and annual returns with HMRC. It will also require significant changes to HMRC's own systems and processes.

3.3. We believe that the introduction of basis period reform and MTD for ITSA at the same time represents too much change in too short a period of time, with two large reforms to income tax calculation and reporting in the space of two years. This will place a significant burden on taxpayers and agents, as well as HMRC who will have to not only implement these reforms but also guide and support taxpayers through them. In addition, those who may have made mistakes in implementing the complex transitional rules will not have time to correct these before coming within the requirements of MTD.

3.4. Furthermore, basis period reform and MTD for ITSA will affect many small and unrepresented businesses. While tax professionals will understand the technical aspects of the changes, many of those affected will not and will need help – either from an agent, HMRC or voluntary sector organisations such as the tax charities, which will put an enormous strain on them.

3.5. Ideally, we would like to see more time given to allowing basis period reform to bed in before moving on to MTD. In the absence of this, it will be essential for HMRC to be adequately resourced to assist those taxpayers and agents who need support during the transitional period, to ensure that they apply the rules correctly, and that taxpayers claim the reliefs to which they are entitled. We would also encourage HMRC to take a pragmatic and sympathetic approach to penalties where errors are made by taxpayers as a result of this reform.

Association of Taxation Technicians
23 November 2021

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Note:

The Association of Taxation Technicians

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 over 9,000 members and Fellows together with over 5,000 students. Members and Fellows use the practising title of 'Taxation Technician' or 'Taxation Technician (Fellow)' and the designatory letters 'ATT' and 'ATT (Fellow)' respectively