Introduction of cash basis for unincorporated property businesses
Consultation on draft clauses for Finance Bill 2017
Response from the Low Incomes Tax Reform Group (LITRG)

1 Executive Summary

1.1 We welcome the opportunity to comment on draft clause 1 and Schedule 1 of Finance Bill 2017 which introduce the cash basis for unincorporated property businesses.

1.2 We cautiously welcome the introduction of these new rules, as the option to use a simplified accounting basis may be helpful to landlords with the introduction of Making Tax Digital (MTD), provided it is not too complex to understand, detailed guidance is available to assist unrepresented landlords and it will not result in an overall tax disadvantage.

1.3 As the cash basis becomes the default position from 6 April 2017 for most landlords with rental income under £150,000 it is imperative that clear guidance is provided as soon as possible as some landlords will need to switch from the accruals basis to the cash basis and so will need to consider what changes they may need to make to their record keeping procedures.

1.4 The effect of the transitional provisions on changing from the accruals basis to the cash basis must be clearly laid out in guidance with clear examples to ensure they are properly understood as unrepresented taxpayers may well find the rules difficult to apply.

1.5 We expect the guidance to be available in both digital and non-digital forms, and that some appropriate nudges and prompts will be included in both free and paid for software.

1.6 We welcome the relaxation of the allowable interest restriction when applying cash basis to property businesses, so that deductible interest is to be calculated in the same way as it

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would be under GAAP accounting as this should make the cash basis more attractive to landlords than might otherwise have been the case.

1.7 However it is unfortunate that there is not consistency of approach between cash basis for unincorporated businesses and that for unincorporated property businesses when deciding which basis of accounting to apply, as this introduces a level of complexity which could have been avoided.

1.8 We believe landlords who rent out their homes to pay for residential care fees should be exempt from the MTD programme and would urge that further consideration be given to introducing a specific exemption for this group.

2 About Us

2.1 The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.

2.2 LITRG works extensively with HM Revenue & Customs (HMRC) and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.

2.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

3 General comments

3.1 We cautiously welcome the introduction of these new rules, as the option to use a simplified accounting basis may be helpful to landlords with the introduction of the digital tax programme, provided it is not too complex to understand, detailed guidance is available to assist unrepresented landlords and it will not result in an overall tax disadvantage.

3.2 It must be remembered that most taxpayers, particularly those who are unrepresented, are unlikely to be familiar with the terms 'accruals basis' and 'cash basis' and so all guidance issued in relation to this area must be clear and include helpful examples. Indeed, some taxpayers may be using the cash basis already: for them, this change will simply regularise their position, which is helpful. For taxpayers who are correctly using the accruals basis currently, the main effect of the change of basis of accounting will be one of timing only. Both of these situations should be conveyed clearly in the guidance too.

3.3 The effect of the transitional provisions on changing from the accruals basis to the cash basis must be clearly laid out in guidance with pertinent examples to ensure that rental income is not inadvertently taxed twice due to being included in income for two consecutive years where the earlier year is assessed on an accruals basis and the later year on a cash basis. Conversely, the guidance must also make it clear how to avoid expenses being inadvertently claimed twice.

3.4 We believe that the guidance must be available in digital and non-digital forms, and that some appropriate nudges and prompts should be included in both free and paid-for software. This will assist unrepresented taxpayers in particular to make an informed choice as to which basis of assessment is best for them.

3.5 We are pleased to note that an election can be made for the property business to prepare its accounts in accordance with GAAP under new s271A(9) ITTOIA 2005 after the end of the tax year, thereby maintaining flexibility and choice for taxpayers. The process for doing this must be clear and straightforward.

3.6 We are also pleased to note the relaxation of the allowable interest restriction when applying cash basis to property businesses, so that deductible interest is to be calculated in the same way as it would be under GAAP accounting for property businesses. Indeed we would be pleased to see this change made to the cash basis for unincorporated businesses too, to remove one of the disincentives in relation to its use.

3.7 However it is unfortunate that there is not consistency between applying the cash basis for unincorporated businesses and applying it for property businesses as the fact that you must elect for it in the former circumstance but it is automatic in most instances in the latter circumstance will almost certainly lead to unnecessary confusion.

3.8 As explained in our response[1] to the consultation 'Bringing business tax into the digital age' we believe landlords, many of whom will be elderly, who rent out their homes to pay for residential care fees should be excluded from the MTD programme and would urge that further consideration be given to introducing a specific exemption for this group.

LITRG
28 February 2017

[1] http://www.litrg.org.uk/latest-news/submissions/161108-making-tax-digital#toc-bringing-business-tax-into-the-digital-age