Reforming the cash basis expenditure rules
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 the draft clauses for Finance Bill 2017 in relation to reforming the cash basis capital expenditure rules (section 33A, Part 2, of the Income Tax (Trading and Other Income) Act 2005 (ITTOIA 2005)).

1.2 We welcome the introduction of these new rules, as we think they will be helpful for low-earners who may struggle to understand the current rules when applying the cash basis to new capital purchases. These new rules add some simplification while not introducing substantial changes that are likely to result in the self-employed who use the accruals basis (whether by choice or because they are unable to use the cash basis) being at a tax disadvantage.

1.3 As these new rules are being introduced from 6 April 2017 it is crucial that clear guidance is provided as soon as possible as the self-employed will need to consider whether they are keeping their business records using the cash basis or the accruals basis and to understand how to account for capital expenditure.

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

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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 welcome the introduction of the reforming of the cash basis capital expenditure rules. As the cash basis is viewed as a simpler accounting basis for some smaller businesses, it is sensible to consider changing the more complex areas of business tax where appropriate. The treatment of capital purchases is an area of tax which many small businesses struggle to understand and are very likely to make genuine errors when completing their tax returns. We welcome amendments which simplify this tax treatment so it is easier for unrepresented taxpayers to understand.

3.2 We are hugely concerned that clear and detailed guidance will not be available and publicised before the introduction of these rules on 6 April 2017. As businesses may keep different business records depending on whether they use the cash basis or the accruals basis it is important that they are made aware of the changes before the start of the tax year, something which may prove to be difficult to achieve.

3.3 It is particularly important that clear guidance is produced in a variety of formats with unrepresented taxpayers in mind and that the guidance explains what capital purchases will not qualify for treatment under the cash basis. For example, the guidance should explain and provide examples on what expenditure is capital or revenue, what are depreciating assets and financial assets, and how cars and motorcycles should be treated if the cash basis is used. The guidance should also help all taxpayers by pointing out other available tax reliefs, such as the simplified expenses tax relief for business mileage and the tax relief available for work-related training. We strongly recommend that software contains nudges and prompts explaining the different tax consequences when making decisions on which accounting basis to use.

3.4 The draft legislation allows taxpayers who will be disadvantaged by these new rules to use the old rules for the 2017/18 tax year. We are concerned that small unrepresented businesses will not have the appropriate understanding to make the best decisions and this could result in them being at an unfair tax disadvantage when compared to businesses who are well able to afford professional advice. Guidance should include examples explaining where taxpayers may be disadvantaged when comparing the old and new rules to decide which would be the most beneficial for their own tax position. As the Government is concerned that these new rules could cause a tax disadvantage we recommend that the purchase of a capital asset is included as a commercial reason to move from the cash basis to the accruals basis.

3.5 We request confirmation that any changes to the cash basis will mirror the rules for the cash basis used by the Department for Work and Pensions (DWP) for self-employed universal credit (UC) claimants. The two systems currently differ and we consider it essential that there is complete alignment between the information that claimants must provide to DWP for UC claims and to HMRC for tax reporting purposes.

4 Comments on draft legislation

4.1 ***Section 33A ITTOIA 2005***

4.1.1 No comments.

LITRG
24 February 2017