

**Increasing cash basis thresholds for unincorporated businesses
Consultation on draft Statutory Instrument: The Income Tax (Relevant Maximum for
Calculating Trade Profits on the Cash Basis) Order 2017
Response from the Low Incomes Tax Reform Group (LITRG)**

1 Executive Summary

- 1.1 We welcome the opportunity to comment on the draft Statutory Instrument: The Income Tax (Relevant Maximum for Calculating Trade Profits on the Cash Basis) Order 2017.
- 1.2 We understand that the Government wants to encourage small businesses to use the cash basis as this may assist with quarterly reporting under the proposed Making Tax Digital for Businesses. However, we remain concerned that until there is full alignment between the cash basis used for reporting tax to HM Revenue & Customs (HMRC) and the cash basis used by the Department for Work & Pensions (DWP) for self-employed universal credit (UC) claimants, then there will still be a significant additional administrative and cost burden on UC claimants.
- 1.3 As these new rules are being introduced from 6 April 2017 it is crucial that guidance and publicity about the increased thresholds are provided as soon as possible as landlords and the self-employed will need to consider whether to keep their business records using the cash basis or the accruals basis at or before the start of the new tax year. The guidance should ideally provide detailed worked examples showing transitions from the accruals basis to the cash basis and vice versa.

2 About Us

- 2.1 The 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 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 The increase in the cash basis thresholds will allow more small businesses to be able to choose to use this method of reporting their taxable profits. While we recognise that the cash basis is a simpler accounting basis for some small businesses, it will not be the most appropriate method for all businesses, for example if they are loss making or have finance costs above £500 per annum. We recommend that guidance on the new thresholds explains both the accruals basis and the cash basis and when it may be appropriate to use each method of accounting.
- 3.2 We are hugely concerned that guidance on the increased thresholds will not be available and publicised before the introduction of these rules on 6 April 2017. As businesses and landlords 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.
- 3.3 It is particularly important that clear guidance is produced in a variety of formats with unrepresented taxpayers in mind. We recommend that free software, such as HMRC's self assessment online, contains nudges and prompts explaining the different tax consequences when making decisions on which accounting basis to use.
- 3.4 The Explanatory Memorandum states that increasing the cash basis thresholds will 'make it easier for them to provide information' and 'reduces burdens on business and facilitates the introduction of making tax digital'.¹ We agree that this may reduce the administrative

¹ Explanatory Memorandum to The Income Tax (Relevant Maximum for calculating trade profits on the cash basis) Order 2017(Paragraph 7.2):

burden for some businesses but we are concerned that as the cash basis is not fully aligned with the monthly cash basis reporting for DWP for self-employed UC claimants this will continue to be a significant time burden for some UC claimants. We strongly recommend that this matter is addressed as soon as possible in order to reduce the administrative burden and potential reporting errors as UC claimants may get confused between the different rules, different jargon and explanations and using different IT systems.

- 3.5 As the exit threshold will be increased from £166,000 to £300,000 it may be the case that the cash basis is no longer appropriate for some businesses because more detailed financial accounts are required for banking or shareholder purposes. Therefore, we recommend that the commercial reasons HMRC accept in order to change from the cash basis to the accruals basis should include the requirement for more detailed financial accounts.
- 3.6 We recommend that the entry and exit thresholds are reviewed annually, even though under the draft legislation the entry threshold cannot be lower than the VAT registration threshold and the exit threshold cannot be lower than twice the VAT registration threshold. We agree with the ongoing monitoring of the cash basis as stated in the Explanatory Memorandum.² Regular reviews of the size of businesses using the cash basis will provide useful guidance when considering whether to change the entry and exit thresholds in the future. It would be useful if this information was available publicly.

4 Comments on draft Statutory Instrument

4.1 *The Income Tax (Relevant Maximum for Calculating Trade Profits on the Cash Basis) Order 2017*

- 4.1.1 No comments.

LITRG
24 February 2017

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/587782/EM_Extending_Cash_Basis_Threshold_Final_.pdf

² Explanatory Memorandum to The Income Tax (Relevant Maximum for calculating trade profits on the cash basis) Order 2017(Paragraph 12):

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/587782/EM_Extending_Cash_Basis_Threshold_Final_.pdf