Finance Bill 2023-24 Briefings: Cash basis, evasion and avoidance, information to be contained in returns

Management of taxes **OMB**



19 January 2024

CIOT and LITRG have provided representations to parliamentarians for the Finance Bill 2023-24 Committee of Whole House debate and for the Public Bill Committee. Our previous comments on the draft legislation were reported in November 2023's *Tax Adviser*.

Clause 16 and Schedule 10: Calculation of trade profits, etc. (cash basis)

The legislation removes several restrictions in the cash basis with effect from the tax year 2024/25. In particular:

- The turnover threshold (currently £150,000) will be removed to expand the regime to larger unincorporated businesses.
- The cash basis will be set as the default basis for eligible businesses to calculate taxable profits. Currently, generally accepted accounting principles (GAAP) is the default basis and businesses must elect to use the cash basis. This will be reversed, so that businesses must in future elect if they wish to use GAAP accounting.
- The £500 interest restriction will be removed, thereby allowing businesses to deduct any amount of interest as long as it is incurred wholly and exclusively for the purposes of the trade.
- Restrictions on loss relief will be removed. This means that cash basis losses will be able to be set sideways against general income of the same period or carried back to earlier years. Currently, for businesses which use the cash basis, losses can only be carried forward and set against future profits from the same trade or used when the business stops trading.

CIOT’s comments

The removal of these restrictions is a simplification that may encourage more unincorporated businesses to use the cash basis. The current restrictions around loss relief and interest deductions undoubtedly influence some businesses’ decisions not to use it. However, the cash basis will still not be suitable for all businesses, particularly larger and more complex ones. We are doubtful that removing the turnover threshold will encourage larger businesses to use it.

For small businesses, we are concerned that, in encouraging the cash basis, the benefits of the accruals basis in improving financial literacy for the small business owner may be diminished. There is a lack of awareness of what thecash basis is, particularly amongst businesses that do not have an accountant. Making the cash basis the default could lead to businesses using it where it is not the best option for them. HMRC’s guidance needs to be improved and updated.

HMRC need to be alive to the possibility that some taxpayers may try to abuse the rules once the restrictions are lifted.

LITRG's comments

LITRG are generally supportive of these changes, as making the cash basis the default way to prepare business accounts will formalise the way some low-income unrepresented traders are currently, and technically incorrectly, completing their tax returns. However, we consider that the removal of the turnover threshold will not particularly affect this cohort.

LITRG are concerned that there is poor understanding about the cash basis and have stressed there needs to be improved guidance clarifying areas which low-income unrepresented businesses struggle with, such as the timing of receipts and payments under the cash basis, in particular when trading through digital platforms. Therefore, we are pleased that HMRC recognise the need to update their guidance in this area, particularly for unrepresented taxpayers moving from the accruals basis to the cash basis.

HMRC need to develop a compliance approach for taxpayers who realise they have been preparing their tax returns incorrectly using the cash basis but not electing to do so. We recommend that HMRC apply a sensible and 'light-touch' approach regarding any genuine errors that come to light following the move to these new rules.

The full CIOT briefing can be found here: www.tax.org.uk/ref1282

The full LITRG briefing can be found on the LITRG website under Submissions at: www.litrg.org.uk

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Clauses 31–34 and Schedule 13: Evasion and avoidance

Clause 31 doubles the maximum term of imprisonment for the most egregious tax offences. The CIOT is dubious that the measure will achieve its objective of deterring people from committing tax fraud unless it is prominently publicised and lengthier sentences are actually imposed on those who commit such offences.

Clause 32 and Schedule 13 introduce anew power enabling HMRC to bring disqualification action against directors of companies involved in promoting tax avoidance. Whilst we support this measure and the need to protect taxpayers from promoters, it is essential that it is appropriately targeted and prominently publicised. The problem is that, in many cases, the ‘controlling minds’ behind avoidance schemes are not directors of the companies themselves and instead recruit ‘stooge directors’ in order to conceal their own involvement. We want to avoid a situation where stooge directors, who may lack culpability, takethe fall for those actually promoting the tax avoidance. It is important to understand what impact the government believe this measure will have on these controlling minds.

Clause 33 introduces a new criminal offence for a person who, without reasonable excuse, fails to comply with a stop notice issued by HMRC requiring them to stop promoting a tax avoidance scheme. While we are generally supportive of measures to crack down on avoidance schemes and protect taxpayers, we are concerned that this measure crosses an important constitutional line; namely, that something can potentially become a crime on HMRC’s say-so alone. This is because the decision to issue a stop notice rests entirely with HMRC with no external oversight. To add a higher level of scrutiny into the process, we suggest that HMRC should have to make an application to the Upper Tribunal for ‘judicial’ approval before a notice that carries with it the risk of criminal charges is issued by HMRC.

Clause 34 and associated regulations expand the grounds for immediate removal of gross payment status for sub-contractors in the Construction Industry Scheme (CIS) in relation to cases of fraud in some areas. We believe that this measure will achieve its objective, but it is important that minor VAT errors or delays do not exclude a business from gross payment status.

The full CIOT briefing can be found here: www.tax.org.uk/ref1276

Clause 35: Additional information to be contained in returns under TMA 1970, etc.

Clause 35 is enabling legislation to allow HMRC to introduce regulations that will specify additional information to be collected from businesses and self-employed

people via tax returns. It is expected that the regulations will be published in draft in early 2024 and that they will require businesses to provide the following additional information to HMRC:

- Employers will be required to provide more detailed information on employee hours paid using real time information PAYE reporting.
- Shareholders in owner managed businesses will need to provide the following additional information on their self-assessment tax return:
    - the amount of dividend income received from their own companies separately to other dividend income; and
    - the percentage of share capital that they hold in their own companies.
- Self-employed taxpayers will need to provide information on the start and end dates of their self-employment on their self-assessment tax return.

The CIOT is concerned that the cost to business of providing information on employee hours has been underestimated. We also need to understand why HMRC are collecting the data and what they are going to use it for before we can say whether the legislation will work as intended and whether the additional burden on businesses is proportionate.

HMRC must provide sufficient guidance for taxpayers to understand what is required of them, so that the risk of non-compliance (and incurring a penalty) is minimised.

The legislation appears to leave open the possibility that HMRC may in future decide to widen the data they collect by making further regulations. Any increase in HMRC's data collection powers under this enabling legislation should be consulted on before being introduced, giving particular consideration to the financial impact on businesses and other taxpayers, as well as the need for the data itself.

The full CIOT briefing can be found here: www.tax.org.uk/ref1279

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