

Written evidence submitted by the Institute of Chartered Accountants of Scotland

About ICAS

1. The Institute of Chartered Accountants of Scotland ('ICAS') is the world's oldest professional body of accountants. We represent over 22,000 members working across the UK and internationally. Our members work in the public and not for profit sectors, business and private practice. Approximately 10,000 of our members are based in Scotland and 10,000 in England.
2. The following submission has been prepared by the ICAS Tax Board. The Tax Board, with its five technical Committees, is responsible for putting forward the views of the ICAS tax community; it does this with the active input and support of over 60 committee members.
3. ICAS has a public interest remit, a duty to act not solely for its members but for the wider good. From a public interest perspective, our role is to share insights from ICAS members into the many complex issues and decisions involved in tax and regulatory system design, and to point out operational practicalities.

General comments

4. The Treasury Committee has asked for our initial views on the Budget measures; on the usefulness, reasonableness, effect on business and operational implementation of measures - and the extent to which measures have progressed the areas covered in its report about tax reform, '[Tax After Coronavirus](#)', which was published in March 2021.
5. ICAS welcomes the opportunity to give its views and to respond to this inquiry into the Budget tax measures announced on 27 October 2021. Our assessment may be refined when we have studied the Finance Bill, which is due to be published on 4 November. The Finance Bill has not been taken into consideration in preparing this evidence.
6. As a matter of policy, ICAS does not comment on specific tax rates, although we do comment on the operational and behavioural effects that different rates may have. For example, we have commented below on the likely effect of the increase in employer NICs (announced in September, rather than in the Budget) on the 'three-person problem'.
7. From a tax perspective, it has been difficult to establish any main themes or overarching strategy in the Budget measures. It feels like a 'bits and pieces' Budget. We would like to see the government setting out its long-term strategic approach for different areas of the tax system. The 2010 'Corporate tax roadmap' provides a useful model for setting out future tax policy. We would like to see a new corporate tax roadmap, but also similar strategic plans for other areas including:
 - The 'three person' problem and the future of work.
 - VAT in a post-Brexit world.
 - Capital taxes and their interaction with taxes on income.
 - Devolved taxes and their interaction with UK taxes.
 - Tax and the path to net zero.
8. We would be happy to discuss any of our comments below in further detail.

Comments on specific measures

The full consultation process should be followed – Notification of uncertain tax treatment

9. We remain concerned about the introduction of the notification of uncertain tax treatment (UTT) measure. We have raised various issues in our responses to the two consultations and in comments on the draft legislation and draft guidance. We also gave oral and [written evidence](#) to the House of Lords Finance Bill Sub Committee. Whilst some improvements have been made to the proposals, over the course of the consultation process, significant issues remain.

10. We are pleased to see the Budget announcement that the ‘third trigger’ (the ‘substantial possibility’ trigger) will not initially be included in the regime; as currently drafted it is unclear, highly subjective, difficult for businesses to work with and unlikely to deliver useful notifications for HMRC. We hope that it will be permanently dropped from the legislation – but if this is not the case, it needs to be substantially amended.
11. The UTT measure illustrates the importance of following the full consultation process set out in the [Tax Consultation Framework](#) to improve the likelihood of arriving at a satisfactory outcome. Stage 1 of the process - setting out objectives and identifying options – was omitted for the UTT measure. As a result, other options which would not have imposed unnecessary burdens on all large businesses, never seem to have been properly considered by HMRC, leading to poorly targeted legislation and an unsatisfactory outcome.
12. We continue to believe that the UTT measure imposes unnecessary administrative burdens on the open and transparent majority of large businesses instead of being properly targeted at the uncooperative minority. This could potentially have been prevented if the full tax consultation process had been followed. Stage 1 would have given HMRC the opportunity to set out its objectives alongside detailed background information about the problem it was seeking to address – other options for action could then have been identified at an early stage and given proper consideration.

Basis period reform

13. We believe that basis period reform is sensible in principle. It is a useful simplification for most new businesses, and it is essential to make Making Tax Digital (MTD) for income tax workable.
14. We extend a cautious welcome to the Budget announcement that basis period reform will go ahead. We also welcomed the recent government announcement that the start date for MTD for income tax will be delayed for 12 months – and that basis period reform will not come into effect before April 2024.
15. Concerns remain, however, that reform of basis periods combined with the move to MTD for income tax will be a significant upheaval for some unincorporated businesses. This comes on top of other pressures arising from dealing with the consequences of the pandemic.
16. Basis period reform is likely to have cost implications for some businesses which do not have 31 March or 5 April year ends, as profits for an extended period (up to 23 months in some cases) will be brought into charge in the transitional 12 month assessment period. It was proposed that mitigation through spreading these excess profits over five years would be available – but five years may not be enough in all cases. We have suggested that in exceptional cases (defined by reference to a set percentage increase in taxable profits) spreading over ten years should be available.
17. We expect that some businesses will choose to change their accounting dates to 31 March or 5 April but those businesses which cannot do this will have an increased administrative burden going forward, due to the need to apportion profits. Businesses with accounting dates later in the tax year will be particularly badly affected because in addition to apportionment, they will also have to complete their tax returns with provisional figures initially – with amended returns being submitted when the final figures for the second accounting period are available. Partnerships will have to submit amended returns both for the partnership and for individual partners. We have suggested that some of the negative impact could be avoided if businesses were permitted to adjust the provisional figures in the tax return for the next year, rather than by amending the current return.
18. HMRC estimates that 7% of sole traders and 33% of trading partnerships do not currently have a 31 March or 5 April year end. It is unclear how many of these will be able to change their accounting date. Whilst some of these businesses will be large partnerships which are part of multinational organisations (and need to use a common accounting date), others will be smaller businesses which cannot change their accounting date for commercial reasons. Businesses in the farming, tourism and hospitality sectors, some of which will be very small and may have difficulty

coping with the additional burdens, are some of those most likely to be using other accounting dates (30 September or 31 December).

19. We hope that the one year delay will be used for further consultation and the identification of various mitigations (like those outlined above), for businesses which will not find basis period reform straightforward.
20. Ideally, we believe that basis period reform would be introduced and allowed to 'settle down' for a period, before the introduction of MTD for income tax. The current timetable does not envisage such a gap – so a great deal will need to be accomplished in a very tight timetable.
21. Businesses will require suitable software before they can begin preparing for MTD and before they can join the pilot – but very few MTD software products are currently available. Some software providers are likely to have been waiting for certainty about basis period reform (and the mandatory start date for MTD) before finalising their products. It is important that HMRC works with software providers to ensure that a range of suitable software is available in time for all businesses (which want to do so) to join the MTD pilot for a full year ahead of the mandatory MTD start date.
22. MTD for income tax regulations were laid in September, but we assume that these will now be revised to take account of basis period reform – we hope that this will address some of the problem areas identified, particularly around year end finalisation processes and the interaction with self assessment.

Research and development (R&D)

23. We note that the Budget proposes two changes to R&D tax relief with a view to encouraging additional investment in research and development. One change is to extend the definition of qualifying R&D to include cloud and data services.
24. We receive considerable feedback from our members, expressing concerns about the activities of some R&D claims 'specialists' who offer to make R&D claims for clients, in some cases where it does not appear that R&D within the meaning of the legislation is taking place. Some of these advisers pursue aggressive claims (often with fees based on a percentage of the claim). The proposals in the Budget to extend the eligible qualifying expenditure, may well intensify the problem by encouraging more claims.
25. Such aggressive R&D claims may at best be questionable; at worst they are fraudulent. There are two aspects to preventing such claims:
 - Additional HMRC compliance activity so that more of the dubious claims are stopped and advisers are deterred from submitting them because there is a better chance that they will be picked up.
 - The ability to give advice or make claims should be restricted to those who meet the standards that apply to tax advisory work set out in PCRT (which now includes [topical guidance on R&D](#)). In our view, R&D firms (whether claims service or advisory) are giving tax advice – they are advising on how much R&D to claim in accordance with tax law.
26. Addressing the issue of who is permitted to give tax advice is part of the work that HMRC and the government have been conducting into 'raising standards' in the tax advice market. However, it may be that certain niche areas of tax advice, such as R&D claims services, should be used as the basis of a test scheme for regulation, particularly if the Budget measure encourages additional investment in R&D and generates more claims.

Tax administration

27. It was announced in the Budget that legislation will be included in the Finance Bill 2021/22 to 'put beyond doubt' that HMRC may use 'discovery' assessing powers to recover certain tax charges such as the High Income Child Benefit Charge (HICBC), Gift Aid donations and certain pension charges.

28. One of the main reasons behind this measure is the decision of the Upper Tier Tax Tribunal in a recent case. The Tribunal found that HMRC did not have the power to recover an individual's HICBC by issuing a discovery assessment under section 29(1)(a) of the Taxes Management Act 1970, where that individual had failed to report their HICBC to HMRC and failed to file a tax return for the relevant tax year.
29. Whilst the Tribunal accepted that the individual was still liable to HICBC, it concluded that the assessments were not validly raised. We understand that the case is being appealed by HMRC but in the meantime, this measure should address the immediate problem.
30. However, it fails to address the much wider problem which arises because the Taxes Management Act 1970 (TMA) is no longer fit for purpose. There has been no consolidation since 1970 and legislation dealing with tax administration is now scattered across TMA and various other statutes and regulations. It is difficult for taxpayers to understand and apply the legislation to their own tax affairs, or to appreciate the powers HMRC can exercise and any safeguards which exist. The legislation is also not keeping up with technological developments or with new approaches to taxation (HICBC is effectively a mechanism for reducing the child benefit paid to higher earners rather than a 'normal' tax).
31. This is not the first time an unsatisfactory sticking plaster has had to be applied to address a problem with the creaking tax administration legislation. Finance Act 2020 included a section to put beyond doubt that HMRC's use of large-scale automated processes is, and always has been, in line with the law – also introduced in response to taxpayer challenges to the legal validity of HMRC's approach.
32. We strongly believe that the time has come for a consolidation of all tax management and administration provisions in a new Taxes Management Act. Piecemeal attempts to patch up the system, such as this measure (and the similar one in Finance Act 2020), do not address the underlying problems. The opportunity could also be taken to rewrite the legislation in the more user-friendly style adopted by the Tax Law Rewrite project.

Capital Taxes

33. We welcome the Budget announcement that legislation will be introduced in Finance Bill 2021/22:
- to extend the time limit for delivering returns of UK residential property disposals (and paying the CGT) from 30 days to 60 days; and
 - to clarify (for UK residents) that where a gain arises in relation to a mixed-use property that only the portion of the gain that is the residential property gain is to be reported and tax paid.
34. HMRC's UK Property Reporting Service has caused problems for agents and their clients ever since its introduction, not least because the process for giving agents access to clients' property accounts is complicated, time consuming and sometimes does not work. Difficulties have also emerged where CGT on the disposal of residential property has been overpaid but cannot automatically be offset against self assessment liabilities (the two systems are not integrated).
35. Whilst the extension of the time limit does not address all the problems arising from a poorly designed system which does not interact properly with the self-assessment system, it does at least allow more time for taxpayers to consider whether they might need to report, take advice, authorise an agent (where relevant) and file the return - before penalties become an issue.
36. We would like to see lessons learned from the problems which have arisen with the UK Property Reporting Service (and the problems encountered previously with the Trust Registration Service) – and applied to the design of any future tax reporting and registration systems.
37. Extending this time limit was one recommendation made by the Office of Tax Simplification (OTS) in its second report on capital gains tax. The OTS has produced several reports in the last few years, into both CGT and inheritance tax (and the interaction between the two):
- [Office of Tax Simplification: Inheritance Tax Review - first report: overview of the tax and dealing with administration](#) (November 2018).

- [OTS Inheritance Tax review – second report: Simplifying the design of Inheritance Tax](#) (July 2019).
- [Capital Gains Tax review - first report: Simplifying by design](#) (November 2020).
- [OTS Capital Gains Tax second report: simplifying practical, technical and administrative issues](#) (May 2021).

Two suggestions from the first report on IHT (administration) have been adopted – and the recommendation on the time limit for property reporting from the second CGT report has now also been taken up. It is not clear whether the government intends to adopt other useful suggestions from the OTS for administrative changes to CGT and IHT which would help to make these taxes work more effectively.

38. As set out in our general comments, this is also an area which would benefit from publication of a government roadmap, setting out its strategy for capital taxes and their interaction with taxes on income.
39. We will be interested to see whether there are any further announcements (or the issue of any consultation documents) on the forthcoming 'Tax Day'.

The three-person problem

40. The Treasury Committee report 'Tax after Coronavirus' discussed the 'three-person problem' and called for major reform of the tax treatment of the self employed and employees to address it.
41. A key aspect of the problem arises because users of workers' services want to avoid the cost of employers' NICs (and of giving workers employment rights). Sometimes this leads to workers being forced into false self-employment or into setting up their own personal service companies. The off payroll working rules are an attempt to address some of the revenue losses, but do not address the underlying issue and have added considerable complexity.
42. This Budget does not address the problem; rather, it is likely that the 'three-person problem' will be made worse with the increase in employers' NICs that was announced in September 2021 ahead of the Budget. From April 2022 NICs for working age employees, self-employed and employers is to be increased by 1.25%. They will return to 2021/22 levels from April 2023 but at that point the Health and Social Care Levy will be introduced to replace the NIC increase. There will therefore be an increase in the costs of employing workers (compared to using someone self employed) – with a 15.05% employers' rate of either NICs (or NICs plus Health and Social Care levy).
43. We were also disappointed that no further action was announced to take forward the government's 2018 Good Work Plan. The plan stated that the government would bring forward detailed proposals on how employment status frameworks for employment rights and tax could be aligned. The plan also committed the government to legislating to improve the clarity of the employment status tests. Again, we will be interested to see whether there are any further announcements on 'Tax Day'.

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