



Office of Tax Simplification

**Simplification of the
Corporation Tax computation**

11 January 2017

About ICAS

1. The following submission has been prepared by the ICAS Tax Committee. The ICAS Tax Committee, with its five technical sub-Committees, is responsible for putting forward the views of the ICAS tax community, which consists of Chartered Accountants and ICAS Tax Professionals working across the UK and beyond, and it does this with the active input and support of over 60 committee members. The Institute of Chartered Accountants of Scotland ('ICAS') is the world's oldest professional body of accountants and we represent over 21,000 members working across the UK and internationally. Our members work in all fields, predominantly across the private and not for profit sectors.
2. 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 in the many complex issues and decisions involved in tax and financial system design, and to point out operational practicalities.

General comments

3. ICAS welcomes the opportunity to respond to the OTS review of 'Simplification of the Corporation Tax computation' call for evidence, issued in November 2016. We were also grateful to meet with the OTS to discuss this review.

Specific questions

Question 1: Adjustments between accounting profit and CT profit

a. Considering these adjustments, where does the burden feel disproportionate to the outcome or value?

4. For 'small companies' (to be defined, but perhaps those under the audit exemption threshold) it would be a welcome simplification to align accounting and taxable profit more closely.
5. There should be a materiality level for tax adjustment for all companies. The effort required to make adjustments for small items, such as low levels of entertaining expenses, is disproportionate to the benefit.
6. A materiality limit could be set by percentage of profit or turnover, or by fixed limit.
7. With lower CT rates, the impact on tax yields of any changes is reducing. It can be time consuming to explain to business owners why some costs are disallowed for tax purposes, when, from their angle, they are business expenses and the impact is minimal. Difficulties include specific manner of provision of an annual staff party.
8. Significant abuses of the system are likely to emerge in other ways, such as via VAT inspections.
9. Interaction with Money Laundering rules needs to be considered. Professional firms face ML exposure risk where client firms incorrectly claim tax deductions for disallowable expenses, even where these might not be considered 'material' from an accounting viewpoint.

b. Which adjustments are not clear in their purpose, or don't fully align with business activities?

10. Business and staff entertaining rules can be an issue.

Question 2: Relieving or incentivising capital expenditure

a. What key improvements could be made to simplify the current system and ease the administrative burden?

11. Aligning tax and accounting treatment would be a significant easement.
12. While aligning relief for capital expenditure with accounting treatment might seem a dramatic change, as SME companies will largely obtain 100% relief through AIA the risk of accelerating tax relief through differential rates is limited.
13. Company decisions on how to acquire assets depend on more than tax. The tax impact of different financing arrangements means that capital allowance availability is not the only determinant.
14. Companies may wish to retain the asset value of the balance sheet, so gaining tax relief sooner is not the only issue when deciding on depreciation / amortisation rates.

b. Do you think the current system incentivises businesses, or could this be done in a different way?

15. For SME companies the incentivisation seems limited.

Question 3: The 'Schedular' system

a. Are there any particular obstacles to its removal that we need to consider?

16. The scheduler system seems outdated and its removal would be simplification.

Question 4: Making Tax Digital - opportunities for a simpler regime?

a. With a particular focus on the CT computation process, what simplifications could be introduced to make the most of MTD and help its implementation?

17. Cash accounting would bring simplification and more meaningful quarterly updates under MTD, but seems inappropriate for all but micro-business.
18. Alignment of accounting profit and taxable profit would be beneficial, facilitating quarterly reporting.
19. Expense categories should be determined by business information needs rather than taxation.

Question 5: Reporting and compliance processes that could be simplified

a. Are there aspects of reporting and compliance that could be simpler?

Please see attached Appendix A, for two specific examples.

b. What are the benefits vs the risks of simplifying these processes?

20. On a more general note, given that significance of the CT yield compared to the total tax contribution of the largest companies is declining¹, benefits of simplification would appear to outweigh risks.
21. The dynamics for smaller companies may differ, but overall, CT is less significant than, say, payroll taxes.

¹ <http://www.the100group.co.uk/~media/Files/T/The-Hundred-Group/Attachments/Documents/2014-ttc-survey-for-the-100-group.pdf>

22. More frequent digital reporting will be more feasible the closer accounting and taxable profits converge.

Question 6: Simpler tax for smaller companies

a. Could the complexity of the CT computation for smaller companies be almost entirely removed, whilst retaining a clear and simple set of incentives such as AIA? What benefits and concerns would this give rise to?

23. There would seem to be little risk to simplifying the CT computation for smaller companies.

b. Could smaller companies operate a cash based system? What problems would this create? Would cash basis remove the need for AIA?

24. As noted above, cash accounting would be inappropriate for most companies. All but micro entities need accruals accounting for business purposes – calculating profitability, making business decisions, supporting borrowing and complying with accounting standards.

c. Can we create a more appropriate series of definitions for small or simpler businesses, to better target policies and processes according to different needs and circumstances? Where would the boundaries be?

25. Given overall comments at 31 above, some degree of simplification may be appropriate for most companies.

26. If there is to be a separate set of rules for 'smaller companies' it would make most sense for this to be one of the existing limits, such as the audit threshold.

d. What are the implications of simpler CT for unincorporated businesses, where the rules read across to income tax, and how could these be addressed?

27. Taxation of unincorporated business is more complex, involving income tax, National Insurance and CGT; as well as the interaction of personal reliefs from rent-a-room for traders to personal allowance.
28. The impact of simplification on tax yield is likely to be more significant for unincorporated businesses. Simplification for CT need not be read through into unincorporated businesses, though an assessment of the impact of simplification on CT might support changes to taxation of unincorporated businesses.

Question 7: Streamlining tax processes for large and complex companies.

a. Our report identifies some priority areas for simplification: do you agree with this list (in paragraph 2.53) and are there other areas that you think should be included in our review, and why?

29. The list at 2.53 seem reasonable.

Question 8: International aspects

Are there any international comparisons that can be made or case studies that we can learn from where other regimes have implemented simplifying changes to their CT systems?

30. No further comments

Appendix A

Trade/assets previously owned by another group company

1. One specific example is the complexity of treatment of intangible assets in hive-downs. For example, a trading holding company wanting to dispose of the trade, may wish to transfer the trade to a new subsidiary: the new subsidiary being sold on to a third party.
2. In such cases, Substantial Shareholding Exemption (SSE) can remove a charge on tangible assets, but not intangibles. A charge may arise, for example, on transferred goodwill under s780, CTA 2009.
3. This is in contrast with a pre-FA2002 trade transfer under s171 CGTA 1992 in similar circumstances, which would escape a tax charge on intangibles.
4. By way of background, the SSE legislation was amended in Finance Act 2011: the period over which a parent is treated as holding shares in a subsidiary for the purposes of the SSE was extended where that subsidiary's trade/assets were previously owned by another group company. This allow groups to put trading activities into a newly incorporated subsidiary and then sell that subsidiary without share disposal gains being subject to corporation tax. This was a welcome improvement to the SSE regime. However, it has subsequently emerged that there is a problem in the way HMRC interpret the legislation.
5. The 2011 amendment was originally intended to allow a singleton company carrying on several trades in divisions, rather than using separate subsidiaries for each trade, to take advantage of SSE. These companies were at a disadvantage compared to companies which had a separate trading subsidiary for each trade.
6. Yet, HMRC interpret the legislation as requiring that the company must have been a group member before the transfer so a singleton company still cannot qualify. HMRC's Capital Gains Manual specifically states (CG53080C): *"Note that paragraph 15A extends the holding period by reference to the previous use of trading assets by a member of the group while it was a member of a group. Therefore, a capital gains group must have existed at the time. The provision cannot apply where the transferee company is a newly acquired subsidiary of what was previously a single trading company"*.
7. As a result of this approach, singleton companies are still at a disadvantage. Clearly a well-advised company, planning ahead, can address this problem by incorporating a subsidiary for the sole purpose of creating a group – before creating another subsidiary to implement the sale using the FA 2011 rules. However, there is no good reason for this to be required and it simply creates a completely unnecessary complication and administrative burden.

De-grouping charges

8. FA 2011 also changed the rules on de-grouping charges (which arise when an asset is transferred on a no gain/no loss basis to a company that is then sold within 6 years). The change was to treat these de-grouping charges as additional consideration for the disposal in the hands of the seller. This means that the de-grouping charge is effectively extinguished where the disposal qualifies for the SSE. Again this was a welcome improvement to the SSE regime.
9. Unfortunately, the FA 2011 amendment was not extended to the intangible assets regime. This significantly restricts the usefulness of the FA 2011 change to SSE de-grouping charges. It runs contrary to the SSE policy intention of enabling trading groups to make rational business decisions on restructuring, reinvestment and the disposal of shares in trading companies without being discouraged by potential corporation tax liabilities.