Tax Representation

THE INSTITUTE OF CHARTERED ACCOUNTANTS IN ENGLAND & WALES

Tax Faculty

TAXREP 14/04

Key issues for the March 2004 Budget

Letter sent on 8 March 2004 by the President of the Institute of Chartered Accountants in England & Wales to the Chancellor of the Exchequer, putting forward key issues to be addressed in the March 2004 Budget.

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Key issues for the March 2004 Budget

INTRODUCTION

1. On 8 March 2004 the President of the ICAEW wrote to the Chancellor of the Exchequer setting out a number of key issues which we believe need to be addressed in the Budget on 17 March. These specific issues are set out below from paragraph 7 onwards.

2. We also took the opportunity to welcome both the early announcement of the Budget date, and that the date has reverted to mid-March rather than taking place after the new tax year has started.

3. The ICAEW also welcomed further discussion with the Chancellor on any of the issues raised in the letter.

WHO WE ARE

4. The Institute of Chartered Accountants in England and Wales is the largest accountancy body in Europe, with more than 128,000 members. Three thousand new members qualify each year. The prestigious qualifications offered by the Institute are recognised around the world and allow members to call themselves Chartered Accountants and to use the designatory letters ACA or FCA.

5. The Institute operates under a Royal Charter, working in the public interest. It is regulated by the Department of Trade and Industry (DTI) through the Accountancy Foundation. Its primary objectives are to educate and train Chartered Accountants, to maintain high standards for professional conduct among members, to provide services to its members and students, and to advance the theory and practice of accountancy (which includes taxation).

6. The Tax Faculty is the focus for tax within the Institute. It is responsible for technical tax submissions on behalf of the Institute as a whole and it also provides various tax services including the monthly newsletter **TAXline** to more than 11,000 members who pay an additional subscription.

KEY ISSUES FOR THE MARCH 2004 BUDGET

Taxation of small incorporated businesses

7. We remain concerned about the proposed changes, referred to in paragraph 5.91 of the December 2003 Pre-Budget Report to the tax and national insurance position of small incorporated businesses to ensure that the 'right amount of tax' is paid by owner managers on the profits extracted from their companies.

8. We expressed our concerns with this statement in a letter sent by the Chairman of the Tax Faculty to the Paymaster General (published as **TAXREP 46/03**). We would like to repeat the key concerns we expressed in our earlier letter, namely that:

- owner managed companies need certainty so that they can plan;
- it is vital that there is proper consultation on any proposals; and
- if there are to be changes that these should not be introduced until April 2005.

Relief for disincorporation

9. Government policy in recent years has had the result that many previously unincorporated businesses have now been incorporated. We note that on average during this year, incorporations are running at a rate of around 7,500 per month. The likely changes to the tax rules for small incorporated businesses outlined above may mean that many such businesses might be better off undertaken in an unincorporated form.

10. Our view is that the precise form of the business structure should be dictated by commercial rather than tax reasons. Further, the tax system should not penalise businesses that wish to restructure for commercial reasons. The UK tax system includes reliefs that enable businesses to incorporate without suffering immediate tax charges. However, there are no reliefs for companies that wish to disincorporate.

11. There has been detailed consultation in the past about the need for disincorporation reliefs but nothing has ever come of the proposals. We believe that the time has come to consider introducing specific disincorporation reliefs so that incorporated businesses can restructure for commercial reasons without facing prohibitive tax charges.

Pre-owned assets

12. We responded to the December 2003 consultation paper on this issue. This is our paper **TAXREP 09/04**. We accept that questions of tax policy are entirely a matter for Government to decide. However, we believe that it is wrong in principle to rectify a defect in the Inheritance Tax (IHT) rules by introducing an income tax charge.

13. We would like to understand the Government's concerns about the existing Gift with Reservation (GWR) rules and in what circumstances the

Government believes that they do not operate as intended. If the Government is concerned that arrangements are being effected to get round the GWR rules, then we believe that the GWR rules should be strengthened.

14. The proposal to introduce a totally different tax charge appears to be retrospective, unfair, arbitrary and unworkable in practice. If implemented as suggested, it will cause considerable hardship for those who entered into tax transactions many years ago and who will now need to unwind their affairs. It could also result in transactions being subject to both IHT and income tax.

15. We urge the Government to reconsider the underlying policy behind these proposals and instead bring forward properly targeted measures to strengthen the GWR rules. We are very happy to explore with the Inland Revenue ways in which the existing GWR rules could be strengthened to address these concerns.

Pensions and savings

16. We remain concerned that the Government needs urgently to reinvigorate long-term saving and pension provision. Whilst we support much of the thrust of the Government's proposals, in particular the move to simplification, the fact is that few citizens use up their full pension entitlement under the existing rules. The proposals by themselves are therefore unlikely to encourage pension saving.

17. The Government needs to provide real incentives for those on lower and middle incomes to save. Pension provision is only one part of long term saving and more needs to be done to encourage saving in its widest sense, for example, there is concern that the present complicated rules for individual savings accounts deter savers. We understand that a review of this area is under way and we would be happy to contribute to it.

Anti-avoidance legislation

18. Whilst we understand the Government's desire to counter extreme and aggressive forms of tax avoidance, we are concerned that some recent anti-avoidance legislation is so widely drafted that it catches many innocent transactions. Recent problem areas in VAT include the rules for imposing joint and several liability where 'missing trader fraud' is suspected. This is a well intentioned idea but as outlined in the recent decision of *R (on the application of Federation of Technological Industries and others) v CCE* [2004] EWHC 254(Admin), there are doubts as to whether these rules operate as intended as they may infringe EU law.

19. Another example is the proposals for pre-owned assets already mentioned above.

20. It is important that anti-avoidance legislation is properly targeted and is proportionate to the problem being addressed.

FJH
8 March 2004