

TAXREP 1/07

TAX LAW REWRITE: BILL 4: INCOME TAX ACCRUED INCOME SCHEME

*Memorandum submitted in January 2007 by the Tax Faculty of the Institute of
Chartered Accountants in England and Wales in response to
Paper CC/SC(06)20 issued in December 2006 by
HMRC Tax Law Rewrite Team*

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Tax Representation

TAX LAW REWRITE: BILL 4: INCOME TAX

ACCRUED INCOME SCHEME

INTRODUCTION

1. We welcome the opportunity to comment on Paper CC/SC(06)20 (The Income Tax Bill (formerly Bill 4): Accrued Income Scheme) published on 15 December 2006 by HMRC's Tax Law Rewrite team at <http://www.hmrc.gov.uk/rewrite/index.htm>.
2. Details about the Institute of Chartered Accountants in England and Wales and the Tax Faculty are in Annex A. Our Ten Tenets for a Better Tax System which we use as a benchmark are summarised in Annex B.

GENERAL COMMENTS

3. We commented on the draft AIS clauses when first introduced in Exposure Draft No. 8 (October 1999) but, in view of their withdrawal, did not comment on those clauses as amended, pending consultation on their reform, and published in March 2004 as Chapter 7 of Part 4 of the draft Income Tax (Trading and Other Income) Bill (subsequently ITTOIA 2005).
4. As part of our review process now, we have compared the March 2004 draft clauses with the clauses in Paper CC/SC(06)20 and reviewed the changes (as set out in Annex A to that Paper, which we found helpful) in the context of past consultation.
5. The clauses are now presented as a Part of Bill 4, comprising three Chapters, having previously been incorporated as Chapter 7 within Part 4 of the March 2004 Bill. We are content with the structure of the new Part, the clauses being substantially the same as those of March 2004. Whilst the changes to the March 2004 clauses, as set out in Annex A to Paper CC/SC(06)20, are numerous they are mostly relatively minor, being mainly consequential on subsequent legislation or to improve clarity. Specific comments now arising are set out below.
6. We agree the seven Changes proposed, which all appear to be appropriate.
7. The consultation process on the rewrite of the AIS clauses has been disrupted by the ongoing consultation regarding their reform and the difficulty (continuing still) in determining how to reform them. This caused some disruption to the progress of the Income Tax (Trading and Other Income) Bill, but was handled acceptably with due consultation; but the recent decision to add the AIS clauses at Bill 4's Joint Committee stage, with consultees' responses called for by 5 January 2007, has a more severe impact upon the consultation process for both consultees and the Tax Law Rewrite team. The decision to include the AIS clauses in Bill 4, whilst sensible (as the last rewritten Income Tax Bill available), should have been taken earlier.

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SPECIFIC COMMENTS ON DRAFT LEGISLATION

cl 14 Making accrued income profits and losses: general rule

8. Would a signpost to clause 24(2) (Excluded persons: disregard of certain payments and transfers) be helpful to the reader?

cl 16 Making accrued income profits: settlement day outside interest period

9. Would a signpost to clause 24(3) (Excluded persons: disregard of certain payments and transfers) be helpful to the reader?

cl 19 Payment on transfer without accrued interest

10. (4) We agree the amendment to clause 19(4), as set out in Explanatory Notes paragraph 102. Accordingly, in Explanatory Notes paragraph 108, should the reference to subsection (4) be deleted?

cl 23 Accrued income losses treated as payments in next interest period

11. (2) With reference to Explanatory Notes paragraphs 124 and 125 if an interest payment day (exceptionally) is more than 24 months after the previous one, it appears that the effect of clause 23(2) will be to treat a payment treated as made in the first 12 months as being a payment made under clause 23(2) in the second 12 months. As that period will not end with an interest payment day, clause 23(2) then appears to apply again (and, if necessary, successively) to relocate the payment to an interest period which does end with an interest payment day (so that clause 63 then applies). If this is correct, is Explanatory Notes paragraph 125 drafted sufficiently clearly to explain this possible situation (however unlikely it may be in practice)? At present Explanatory Notes paragraph 125 refers to 'the next interest period' which could be construed as the immediately following interest period only. The actual effect of the legislation is, of course, more important than any explanation of it; but we draw attention to this in passing.

cl 25 Small holdings: individuals

cl 26 Small holdings: personal representatives

cl 27: Small holdings: trustees of a disabled person's trust

12. Would it be clearer to refer to 'the nominal value of *all* securities' in the context of the £5,000 limit? It is clear from the clause 5 definition that 'securities' means 'all securities', as confirmed in the Explanatory Notes (for example, in paragraph 135), and that the £5,000 limit does not therefore apply to each security held; but the reader's focus is likely to be upon the individual security or securities with which he/she is concerned.

cl 37 Owner becoming entitled to securities as trustee

13. In Explanatory Notes paragraph 199, is it correct to refer to '*is or becomes trustee*'? The clause applies only where the owner becomes trustee of the particular securities involved.

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cl 42 Sale and repurchase of securities: supplementary provision

14. Why has draft clause 452(5) in the March 2004 Draft Income Tax (Trading and Other Income) Bill been dropped from clause 42? Are references to securities including a reference to substituted securities now to be left for Treasury regulations to deal with?

cl 65 Unrealised interest received after transfer within Chapter 2

15. (6) Would it be simpler to state that a liability to income tax arises on the excess of the unrealised interest received over the residual value of the interest?
16. With reference to Explanatory Notes paragraph 301, is it correct in principle that the transferee rather than the transferor should be taxed on the excess interest received? Clause 44(2) is only in point because of the failure to pay the interest and, if it had not applied, an appropriately increased payment treated as made to the transferor would have been taxed on the transferor under clause 20(2). What is the situation if the transferee has to repay the excess to the transferor?

DETAILED COMMENTS ON DRAFTING

cl 31 Charitable trust etc

17. In Explanatory Notes paragraph 159, the reference should be to 'Subsection (4)'

cl 51 Trustees' accrued income profits treated as settlement income

18. In Explanatory Notes paragraph 240, in the second line within brackets, 'settler' should be 'settlor'.

cl 52 Relief for unremittable transfer proceeds; general

19. (1)(b)-(d), (5) We are not convinced that drafting to refer to payments and transfers in the plural throughout does improve clarity. We prefer the March 2004 draft Income Tax (Trading and Other Income) Bill clause 463 drafting which distinguishes individual and plural payments and transfers.

20. Similar comments apply to draft clauses 53(1)(b), (c), and 54(1)(b).

cl 65 Unrealised interest received after transfer within Chapter 2

21. In Explanatory Notes paragraph 301, insert 'interest' after 'unrealised' in the second line.

TJH/PCB
5.1.07

ICAEW AND THE TAX FACULTY: WHO WE ARE

The Institute of Chartered Accountants in England and Wales ('ICAEW') 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.

The Institute operates under a Royal Charter, working in the public interest. It is regulated by the Department of Trade and Industry 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, including taxation.

The Tax Faculty is the focus for tax within the Institute. It is responsible for tax representations 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 of the ICAEW who pay an additional subscription.

To find out more about the Tax Faculty and ICAEW including how to become a member, please call us on 020 7920 8646 or email us at tdtf@icaew.co.uk or write to us at Chartered Accountants' Hall, PO Box 433, Moorgate Place, London EC2P 2BJ.

THE TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. **Statutory:** tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. **Certain:** in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. **Simple:** the tax rules should aim to be simple, understandable and clear in their objectives.
4. **Easy to collect and to calculate:** a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. **Properly targeted:** when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. **Constant:** Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. **Subject to proper consultation:** other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. **Regularly reviewed:** the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. **Fair and reasonable:** the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. **Competitive:** tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99; see <http://www.icaew.co.uk/index.cfm?route=128518>.