ICAEW REPRESENTATION 171/16
TAX REPRESENTATION

MAKING TAX DIGITAL: BRINGING BUSINESS TAX INTO THE DIGITAL AGE

ICAEW welcomes the opportunity to comment on the consultation paper *Making Tax Digital: Bringing business tax into the digital age* published by HM Revenue & Customs on 15 August 2016.

This response of 4 November 2016 has been prepared on behalf of ICAEW by the Tax Faculty. Internationally recognised as a source of expertise, the Faculty is a leading authority on taxation. It is responsible for making submissions to tax authorities on behalf of ICAEW and does this with support from over 130 volunteers, many of whom are well-known names in the tax world. Appendix 1 sets out the ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark proposals for changes to the tax system.

We should be happy to discuss any aspect of our comments and to take part in all further consultations on this area.

We have attended a number of meetings with HM Revenue & Customs, HM Treasury and also with Ministers in which we have been able to put forward some key comments and concerns and discuss aspects of the consultation document.

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ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.

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INTRODUCTION

1. ICAEW is responding to the consultation paper Making Tax Digital: Bringing business tax into the digital age published by HM Revenue & Customs (HMRC) on 15 August 2016.

2. To inform our response, we have undertaken a wide consultation exercise with our members through a series of face-to-face meetings, conferences, webinars and articles. We have encouraged members and the businesses they represent to also feedback their own views directly to HMRC, as well as sending copies to the Tax Faculty.

3. In addition, in March 2016, ICAEW commissioned research to uncover how businesses currently keep their accounting records. Further details of this research are set out in Appendix 2. In summary:

- 25% are keeping records electronically using accounting software
- 25% still use a totally paper based system, and
- the remainder use a mix of paper-based and electronic systems (e.g. MS Excel) rather than any accounting software.

This indicates that at least 75% of all UK businesses will need to change the way they keep their records, a number which rises significantly among sole traders and micro-sized businesses.

MAJOR POINTS

4. ICAEW supports the move to a digital tax system. Our members are at the forefront of managing change and moving to digital systems so we support the principle of what the Government is seeking to achieve.

5. A digital tax system fit for the 21st century should be designed and built not just around the needs of HMRC but also the needs of taxpayers and what works best for them. **In short, Making Tax Digital (MTD) needs to be designed as a taxpayer-centric system.**

6. A truly taxpayer-centric system should be designed with a number of key principles in mind, including the need for simplicity, certainty and efficiency in line with our ten principles for a good tax system – for further details see Appendix 1.

7. Taxpayers should not be disadvantaged as compared to the current tax system and it is important that safeguards are built in to ensure this is the case. The move to MTD should be driven by business adopting it because it is cheaper and more efficient, not because they are compelled to do so.

8. Currently, the MTD proposals appear to be directed at what will work best for HMRC, with taxpayers and their agents largely expected to fit around the proposed system. In particular, a key proposal is to require all but the smallest micro businesses to keep their accounting records digitally and submit quarterly reports. While there will be an exempt category of “digitally excluded”, it is likely to be very limited. We think it is wrong in principle that HMRC should be seeking to dictate that businesses should keep their records electronically.

9. It is clear from the results of our survey, referred to above, that any change will impact significantly on the way businesses currently operate and for many small businesses it will mean additional processes and attendant costs.

Key concerns and recommendations

10. We have set out below our key concerns and recommendations as have emerged from consulting extensively with our members.

The business case for MTD has not been made

11. A proper business case needs to be made for MTD, demonstrating clear cost savings to businesses and taxpayers as well as to HMRC. It needs to be based on realistic assessments of transitional and ongoing costs. As it stands, the business benefits of MTD have not been made and all our feedback from members is that the ongoing costs will be significant: they are not convinced that there will be any ongoing cost savings and that if anything compliance costs might be higher than at present.

12. We are happy to work with HMRC to estimate what will be the cost of maintaining digital accounting records and the other obligations. However, we believe that the costs to businesses of implementing MTD as proposed will be substantial. Further, unless MS Excel is allowed as an acceptable way of digital record-keeping and reporting, the costs are likely to be considerably higher than they would be otherwise.

13. While we have not ourselves undertaken a detailed survey of costs, and such evidence as exists needs to be treated with caution, it seems to us self-evident that the need to submit quarterly reports on top of a year end reconciliation (by whatever name called) will increase costs as compared to completing and submitting one annual return. For example, one of our practice members undertook a survey of his firm's SME clients and concluded that the transitional costs for all their clients would be an increase by an average of £1,250 per annum.

14. In the oral evidence that the FSB gave to the Treasury Committee on 27 October 2016, we understand it has undertaken a survey of its members. We understand that the survey has shown that the extra costs for small businesses would be in the order of £2,700 per business.

15. Based on these two estimates of the costs of MTD, they suggest that the true costs for businesses of implementing MTD will be at least £3bn and could be up to £7bn.

16. It is clear that the costs of MTD to taxpayers, and in particular businesses, have not been identified in anything like sufficient detail to justify this change. However, we believe that the costs to businesses of MTD are far higher than suggested. Taxpayers are being asked to fund a £1.3bn investment that will cost them somewhere between £3bn and £7bn to implement, with ongoing costs on top of that. If MTD is made mandatory, it is clear to us that the implementation and ongoing compliance costs will be high with little, if any, cost savings in the short term. Further, these burdens will fall hardest on those businesses which can least afford it.

No mandation at the outset and during the transition

17. Taxpayers and society need to have trust and confidence in the move to MTD and this is likely to be best served by adopting a non-mandatory approach at the outset. There should be no question of mandation during the implementation period. Each part of HMRC's IT system and support function needs to be in place, properly tested and working for taxpayers. This obviates the need to make specific provision for the digitally excluded in the medium term. Once the system is up and running successfully and taxpayers are taking it up then the question of mandation can be reassessed.

If mandation is adopted, the proposed exemption limit needs to be much higher

18. If, in spite of our recommendation in para 17 above, ministers decide to proceed with mandation, there should be an exemption for the smaller businesses. The current proposal for the exemption, set at £10,000 turnover, is unlikely to exempt any taxpaying business, trade or rental. We recommend a much higher level set no lower than the VAT threshold, a long-standing deregulatory limit designed specifically to ease regulatory burdens.

Set a realistic timetable for implementation

19. The current timetable for implementing Making Tax Digital (MTD) is unrealistic and this undue haste is not in the best interests of taxpayers. While we support the move to digital, it will take at least five years to do this properly. Rushing implementation is likely to lead to trouble, not just for HMRC but also for taxpayers and damage the credibility of the UK tax system. A controlled roll-out stands a much better chance of success, with the adoption of a longer timeframe and allowing market take up to increase naturally. If this is not properly implemented, but is done in a rush, confidence in the tax system and in HMRC will be severely damaged and have a knock-on impact on UK tax compliance.

Decouple digital record-keeping from quarterly reporting.

20. In designing and then implementing MTD, government should decouple the digitalisation of record keeping from any quarterly reporting requirement. While the two functions could ultimately be made to work with the right software and skills, a more gradual implementation will be easier to achieve, especially for those whose business administration skills would not easily adapt to embrace an end to end mobile phone App or IT system. In addition, digital exclusion must be appropriately addressed – see our comments below.

Learn the lessons from previous Government IT projects

21. By any standards this is a huge IT project. The cost of this project will have to be met by taxpayers and they need to have confidence that this project can deliver real benefits for them and is value for money. Huge IT projects of this nature are extremely challenging to deliver on time, on budget and with all that they promise. It is important to learn the lessons from previous large Government led IT projects that have not delivered all that they promised, often with considerable sums of taxpayers' cash being wasted as a result.

Digital record keeping will not reduce the tax gap

22. HMRC is hoping that through MTD, businesses will make fewer errors in their record keeping and so the tax gap would be reduced. We support the government's efforts to reduce the tax gap but we are not convinced digitalisation is the answer. In our opinion, using digital tools to record transactions close to 'real time' is more likely to capture previously omitted expenses, while those who suppress sales in an analogue world will continue to try and do so in a digital world. We would welcome the opportunity to explore with HMRC more effective measures to address any perceived deficiencies in business record-keeping.

Review the fundamental principles of financial and tax reporting

23. More generally, MTD offers the UK an opportunity to think carefully about the fundamental principles of financial and tax reporting and record keeping. Accounts are not only used for tax but used by businesses for a variety of purposes. In a system designed around the needs of taxpayers, we should not seek to change the way businesses operate just to accommodate MTD, but instead should consider what change is appropriate in a wider context.

Support the role of tax agents

24. Many taxpayers, especially those with more complicated affairs, use a tax agent. HMRC's emerging data is that agents have a positive impact and improve compliance – in short they make the tax system work and help ensure that over 93% of tax in the UK is collected with little or no input from HMRC. A good agent will help to improve efficiency for the taxpayer and for HMRC and can help address some digital exclusion issues.

25. It follows that MTD should be built around the ability of taxpayers to appoint an agent to act on their behalf and to do everything a taxpayer can do. Tripartite involvement during development of IT is essential. HMRC currently has separate conversations with software suppliers and with agents. Agents and other accounting professionals will be key to making this work and their access to the system must be put in place before the system becomes mandatory.

26. Agents can help to provide additional training and education to taxpayers, but the current timescale and wide scope of MTD coupled with the lack of detail about the precise proposals will make their effective involvement in MTD incredibly challenging. As noted earlier, we believe that MTD should be voluntary, not mandatory, encouraging rather than forcing businesses to do something for which there is no clear business advantage. We recommend that sufficient time is allowed to get this right and which gives agents the opportunity to help support the training and education that will be needed.

Taxpayers need education and support

27. A major change of this nature needs an extensive taxpayer education exercise. Education, both of HMRC staff and of business, must form a key part of any implementation plan, together with an agile approach which has been fully consulted upon and agreed to be achievable.

28. The results of our survey and HMRC's own survey from 2015 suggest that more than half of taxpayers will need help and support with this change. In addition, there is a significant proportion of taxpayers who are digitally excluded.

The needs of the digitally excluded need to be respected

29. However well designed the new system, MTD will not work for all taxpayers. While the figures in para 2.24 of the Making Tax Digital consultation suggest a rosy picture of digital engagement, the picture is more complicated than it appears, not least because much of the digital engagement in VAT and corporation tax is actually through the use of agents: if these are stripped out, it is clear that there is a significant proportion of unrepresented who are not (for whatever reason) digitally engaged.

30. It is important that the system is not forced on those who are not able to comply. A number of studies and surveys undertaken by HMRC in the recent past have confirmed that there is a significant proportion of taxpayers who are digitally excluded. A survey undertaken in 2015 by HMRC highlighted that over half of the self-employed were either digitally excluded or were assisted digital. This can be for a variety of reasons, including poor broadband connectivity, lack of digital skills, education, and lack of confidence or disability. The income tax population is considerably larger than the other business taxes for which definitions of digitally excluded have been set and the solution will need to accommodate this.

Tax simplification should put on hold pending digitalisation

31. The consultation paper *Simplifying tax for unincorporated businesses* (one of the six papers published simultaneously on MTD) proposes measures which might simplify some areas of tax. In principle we support simplification of the UK tax system and moving to digital provides an opportunity to consider this aspect. However, too much change at the same time is not recommended. We strongly believe that these proposals should not be a priority for the government and the focus of attention should be a successful transition to a digital tax system.

32. Moving towards a digital tax system by April 2018 will be a huge transition for many businesses and businesses need to be given time to ease into the new regime without additional unnecessary changes that will overload the tax system. In any event, we think that tax simplification measures should first be reviewed in the light of the proposals made by the Office for Tax Simplification.

Stability and certainty are needed in the transition to MTD

33. We would urge the government to keep as far as possible the structure of the tax base unchanged during the MTD implementation period. The UK tax system is caught in a culture of constant change which increases compliance costs for taxpayers and HMRC while increasing the risk of mistakes and inefficiencies. For example, higher rate tax relief for interest on let property is being phased out and will gradually be given as a basic rate tax reducer rather than as a deduction from taxable income. Such changes add complexity and should be avoided during the implementation of MTD. To help ensure a successful transition to digital, the UK tax system desperately needs a period of certainty and stability.

Review MTD in the light of Brexit

34. Although this consultation was published two months after the EU referendum, there would have been little time to consider how this might affect the proposals. These now need a review in the light of Brexit and the need for the UK to remain a competitive location for inward investment. This will be helped by providing certainty and not loading costs on businesses for the benefit of HMRC rather than the business.

The needs of businesses, including partnerships, need to be addressed

35. There has so far been little mention or discussion of the special needs of a number of business, the most common cited example being partnerships. However, many businesses, especially property businesses, are also run by trustees. More generally, while some of these business arrangements, such as partnerships, have very simple structures, others are very complex. It is essential that adequate consideration is given to the needs of shared business interests. At a very simple level, the quarterly return periods chosen by the representative partner may not suit other partners with other business interests reporting to different periods.

36. At a meeting with HMRC on 31 October 2016, we understand that no one has come forward to develop the software for partnerships – this is a major problem given that the proposed start date of April 2018 is less than 18 months away. Further, although the consultation document (in para 4.39) recognises that partnerships can be ‘complex businesses’, it does not discuss how these are identified nor how they might be dealt with. So, how do we know which partnerships would be included for the start date of MTD and which would be out? We would be happy to work with HMRC on identifying the criteria for inclusion, but in view of the lack of a workable definition for the impending start date of MTD, we believe that the start date for all partnerships needs to be deferred by at least a year and ideally longer.

37. Although a small group there are a significant number of people who do business through Lloyd’s of London either as individuals or through a partnership and it is difficult to see how they will report digitally and they certainly cannot report in real time. Without a clear plan for these individuals there should be no mandation.

38. More generally, individuals with multiple business interests are likely to struggle to use the same quarterly return dates for all their businesses, for example a business running ski holidays in winter, may run a yacht charter business in summer, but using different quarter end dates. This will be exacerbated if they also have income from property.

RESPONSES TO SPECIFIC QUESTIONS

Question 1: What are the challenges for businesses that currently keep their records on paper or simple spreadsheets in moving to an integrated software package for record keeping, and what further measures or support would help businesses to meet these challenges?

Record keeping

39. Paragraph 2.1 of the consultation observes that ‘there is currently no consistent approach to record keeping taken by businesses’. That is hardly surprising given that ‘one size does not fit all’ and the myriad types of different businesses. The starting point is that businesses should keep business records appropriate to their needs, but sufficient to support entries on the tax return and business owners with a professional adviser will be advised accordingly. Many small businesses keep perfectly adequate paper records which are processed periodically by a bookkeeper or Chartered Accountant. As they grow, it may become more cost effective or efficient for them to use a spreadsheet or simple software and the accountant will set this up for them, train them in how to use it and then help as needed. But this will only happen if it is better for the client and for the business.

40. Mandating a move to digital record keeping removes a key element ensuring that business advice focusses on what is best for any particular business. We believe it is wrong in principle for HMRC to seek to dictate the nature and form of how businesses should keep their records.

41. If in spite of this the Government still seeks to insist that all but the smallest businesses must now keep accounting records digitally, there will be a number of other challenges. Clearly, the scale of the challenge will depend on how digital the business is already. Members have described to us how some clients already use an end to end accounting system where little additional help is needed other than at the year end when the accounts are finalised and the tax adjusted figures are simply filed on the return. Others use proprietary software, but only for some aspects of their record keeping. Spread sheets are very widely used, but a large number of businesses require a full bookkeeping service working from paper records.

42. In March 2016, ICAEW conducted a survey researching 500 businesses. Just 25% of businesses surveyed said they manage their accounts electronically using accounting software. The same proportion told us they use a solely paper-based system. The remainder are either using electronic (non-software based) methods or else a mix of these and paper-based management (see Appendix 2 for further details). This means that 75% of businesses will need to change the way they keep their accounting records. This will incur considerable cost, both directly and in time not being spent running the business, for no clear business benefits.

43. We have not attempted to calculate these costs, but they will be considerable and most importantly, some of this cost will be ongoing. We refer to our key comments and recommendations above about the likely actual costs.

44. Many taxpayers will want a full bookkeeping and accounting service to be provided by a third party, eg, a Chartered Accountant. We would like confirmation that this will be possible, even though the hardware and software are provided through the accountant rather than the business.

Choosing software

45. Choosing the right software and hardware, learning how to use it, keeping up to date, helping staff and/or clients to learn new skills and different processes will come at a cost. There are VAT issues to consider, both in applying different tax rules for direct and indirect taxes, and in reporting those differences in-year.

46. For those who already use software, they may need to replace or upgrade that software and hardware. Often this will need to be modified to the needs of the business, especially where work is project based, again requiring time and incurring more costs.

Access to broadband

47. The challenges for some businesses are even greater. For many, obtaining access to broadband is still very difficult; not just any broadband, but genuinely fast reliable broadband. We have had many representations from the farming community and others who live in rural areas on this point. One practitioner is acting for clients in Denbighshire who do not even have mains electricity. And it is not just remote areas where this access is an issue. Generic assurances that the government is supporting investment in broadband provision are insufficient when HMRC is intending to make MTD mandatory for many from April 2018.

Use of Excel

48. In most responses, we have been told that it would be totally counter to exclude the use of MS Excel in any proposal that claims to be improving accounting by business. This is the cheapest and simplest tool of choice for large numbers of businesses; it is flexible and can be used to integrate with other applications for larger businesses or as a stand-alone bookkeeping system for a small business under the supervision of their accountant. It is a vital tool used by many UK businesses in their accounting systems and this should be allowed to continue.

Training

49. Many trades and professions are used to spending time attending regular training courses which have a direct link to the nature of their business. The cost of the course and time away from customer facing work is accepted. However, requiring a plumber, entrepreneur, dentist, architect or freelance editor to spend time installing and then learning how to use the latest version of their accounting software must have a considerable and ongoing impact on GDP.

Numeracy and literacy

50. Furthermore, in any digital world, we cannot ignore the high percentage of school leavers in England with poor levels of functional literacy and numeracy. The recent OECD report, Building skills for all: a review of England highlights that in 2012, there were 'nine million working aged adults in England (more than a quarter of adults aged 16-65) with low literacy or numeracy skills' who 'struggle with basic quantitative reasoning or have difficulty with simple written information'. Many of these will be self-employed and will need considerable assistance if they are to be trained to use even a basic accounting system rather than rely on their accountant.

VAT

51. Finding (and in most cases, paying for) suitable software or apps is likely to be a challenge for most businesses. The problem is more acute for VAT registered businesses where smaller businesses benefit from simplifications, such as the flat rate scheme, cash accounting, margin schemes and annual accounting for VAT. It seems unlikely that these will be fully catered for by basic, free, software and apps.

52. Retailers who use one of the "retail schemes" to work out their output tax liability will also face the challenge of finding (and probably buying) suitable software or apps. Larger retailers, who use a "bespoke" retail scheme agreed individually with HMRC may find this particularly difficult.

53. Businesses that have a mixture of VATable and VAT exempt activities may find it hard to access software or an app that can cope with partial exemption special methods. While it may not be too difficult to incorporate the standard, turnover based, partial exemption method into an accounting package or app, special methods use a wide variety of bases to determine input VAT recovery. Sectorised methods may use different calculations in different sectors – headcounts, transaction counts, space utilisation, individual time records and transaction values might be used and there might be multi-level calculations to allocate input VAT to sectors before the sectorised calculation is made. It seems probable that, as happens now, such calculations will need to be undertaken outside the primary accounting software/app and then fed into it. At present, typically, businesses of all sizes will use spreadsheets to take data from the main accounting system, apply the relevant calculations, and produce figures for the VAT return. Automating that process, and changing it when the business develops and the partial exemption method has to be changed to reflect that, is likely to be difficult and expensive. While it is not without its issues, the use of spreadsheets is relatively simple, flexible and can provide a suitable audit trail to enable validation of the figures produced.

Question 2: What information and guidance would you find helpful in choosing the appropriate software for your business?

54. The current list of commercial software on GOV.UK states simply that their products can submit one or more elements of the tax return and supplementary pages to HMRC and that HMRC will accept valid tax returns, supplementary pages and attachments for the products listed. There are currently 30 suppliers listed and most of these have a number of products and packages available.

55. The UK markets for energy, insurance, pensions, broadband and mobile phones are just some of those which have been criticised for making it difficult for customers to choose a suitable, cost effective product and there is no reason to presume that it will be any easier for the UK's

4.8m businesses to choose between these software products, whether free or otherwise. It is essential that pricing structures are easy to understand and compare.

56. The consultation states that HMRC is currently working with 600 software suppliers. We are concerned that with such a wide variety of suppliers and products in the market, the amount of choice will make it very difficult for a business to choose without help and a subsidiary market offering this guidance could develop, adding yet another layer of cost.

57. The following information, objectively displayed, would be useful when it comes to choosing an application that would meet the MTD needs of a business:

- The cost relative to the size of the business
- The cost and frequency of updates - legislative and software upgrades
- Ease of use
- Its suitability for the specific business activity/income streams being generated by the business
- What additional functions are available, eg, is it possible for a third party or authorised agent to gain remote access to the application? For a Chartered Accountant with clients using different software packages, this will be an important consideration
- How many users does the product allow on one licence?
- Does the product allow a different agent to act for different taxes, eg, income tax and VAT are often handled by different agents
- The compatibility of any hardware and/or software with other locally stored applications or data and any stored more remotely, eg, in the cloud
- The record retention, storage, audit trail etc of the application
- The ability of the application to integrate across a variety of Government Departments
- Whether the application can also produce the reports necessary for universal credit
- Will prompts and tips be free?

58. Businesses will be concerned about whether their commercial software provider will remain in business and their exposure should the software provider fail. It is not clear that a business would necessarily have access to records held in the cloud should this happen. It is also not clear how such records would be accessed by the representatives of a deceased taxpayer, a taxpayer who loses capacity or a taxpayer who simply can no longer afford to pay for the software.

Question 3: What types of business should a free software product cater for? What functionality would be necessary in a free software product?

59. Free software should be available to all businesses, including rental businesses, which are presently below the VAT registration threshold. We have suggested this threshold as the level below which businesses should be excluded from mandation should the government continue to pursue that requirement. If free software was available to these businesses, this would encourage voluntary take-up if it brings them administrative savings.

60. The free software would need sufficient functionality to enable the user to meet any obligation imposed upon them by MTD, such as quarterly returns, amendments to these returns and final submission. For taxpayers with other income, the software would also need to allow this to be pre-populated and returned in the final post year-end tax return type submission.

61. Free software will be needed for sole proprietors, partnerships and trusts. It will also be needed by some agents and family and friends filing on behalf of these entities.

62. Free software products would need to carry some basic levels of assurance:

- How long would they continue to be offered free?
- Will software and legislation updates also be free?
- Would it be possible to move data between suppliers without charge?

- What would happen if the business circumstances change during the year and the specification of the free software becomes insufficient for their needs?

63. While there may be several free products available for a particular set of requirements when MTD is first launched, this may not be sustainable in the medium to long term. A collective decision by the software industry to stop providing free software would be severely damaging to HMRC's ability to collect tax. Will there need to be a minimum number of suppliers below which HMRC is compelled by law to provide its own free product?

64. We are concerned about how VAT will be handled by free software. While online filing of VAT totals each quarter is now the norm for most VAT registered businesses, it will be more challenging to scan, read and store a VAT invoice with VAT information, particularly for a business using one of the simplified schemes. It seems counter intuitive that a taxpayer who is being helped with their VAT accounting should then be denied free software for just that reason.

Question 4: What level of financial support might it be reasonable for the government to provide towards investing in new IT, software or training, to whom should such support be aimed, and what is the most appropriate form for delivering such support?

65. It is becoming increasingly clear that HMRC needs MTD to be mandatory in order to fulfil its business case to support its own investment in new technology. This is a direct transfer of cost from HMRC to business through MTD. We believe this is wrong in principle.

66. Given that conclusion, we believe that the cost of the transition to MTD should be fully deductible as a tax reducer in the year of payment, with a repayable tax credit where there is insufficient tax payable. This would also act as an encouragement for businesses to participate in MTD on a voluntary basis in the early years.

67. Training of different types will need to be available through a variety of media. For taxpayers new to the internet, a very hands on approach will be needed as they will need help to go online or use their phone. Using a phone to make a call or send a text is very different from using a record keeping app, and likely to be much more problematic. Such training needs time to prepare and as we do not yet know the exact requirements, nor do we have access to software or indeed know when it will be available, it is difficult to suggest in detail what will be needed.

Question 5: What other forms of support would help to make the transition to Making Tax Digital easier?

68. New businesses and those new to using software for business record keeping, will always need assistance to get started and then each time something changes. Most accountants already do this for their clients and will be a valuable multiplier to implement MTD. However, the current timetable for implementation makes this task challenging at best and impossible at worst.

69. The consultation (para 2.24) cites the large proportion of businesses currently transacting with HMRC digitally (99% of VAT returns, 98% of Company Tax returns and 85% of self assessment returns filed online) as evidence of the wide ability to acquire and use digital tools. These statistics fail to reflect the large proportion of these returns which are actually filed by agents on behalf of their clients and only a small proportion are supported by digital accounting records. Agents already provide a comprehensive support service to their clients, which has been instrumental in achieving the current proportion of returns filed online. It is vital that, in the move to digital, HMRC does not design a system which makes it more difficult to provide this service. HMRC relies heavily on the business knowledge and accounting support provided to business by Chartered Accountants and this is increasingly important as HMRC staff numbers continue to fall.

70. We would also observe that filing a return online is not the same as keeping accounting records digitally, which is very much more of a real time function.

71. The consultation is silent on whether the requirements will allow paper records to be input to accounting software, say, monthly or quarterly, before totals are transmitted to HMRC, although the implications are that near real time digital record keeping is the intention. If underlying paper records can still be the starting point, then bookkeeping services would continue to be able to assist record keeping. This might be a sensible solution, at least for the foreseeable future while the new system beds down.

72. Much of the education material published so far on GOV.UK is overly simplistic and glosses over likely problems. It is essential that businesses have a ready source of well-trained support staff to help with tax technical and related online filing queries. During the implementation phase of previous moves to online filing, it has not always been clear whether a taxpayer should contact the specific helpline for that tax, eg, self assessment, or the online service helpdesk.

73. Internet access within local libraries and/or post offices would be useful to those with little or no connectivity. However, many taxpayers may be rightly unhappy that they are forced to deal with their private finances in such a public place.

Question 6: What facilities would make it easier and more secure for businesses to enrol for Making Tax Digital and use software regularly?

74. The following factors might help ease the transition to MTD:

- Good broadband coverage with high speeds
- A high degree of confidence in HMRC security systems
- A clear and well defined process with ease of use and access
- The protection of access to personal data in the event of the failure of a third party supplier
- The protection of access to personal data in the event of the taxpayer getting into financial difficulty
- All personal data should be stored on computers located within the UK. This would ensure that the UK courts have jurisdiction over the person or persons storing the data
- Third party software suppliers should be required to retain, and allow the taxpayer access to, stored data for a minimum period, we suggest seven years, after any subscription lapses
- The ability of any contractual terms to be ‘grandfathered’ for example to personal representative’s on the death of the taxpayer, or to an attorney in the case of incapacity
- If possible, a universal standard should be used for stored data such that the data can always be imported by another application should the taxpayer choose to change their supplier or in the event of the failure of the supplier.

Question 7: Do you have any comments about the practicalities of keeping evidence of transactions and trading when using digital tools?

75. We presume that the digital records generated by HMRC approved software will comply with HMRC’s requirements on record-keeping and that the underlying law will reflect that.

76. There could be issues if, say, the scans/digital images are stored on a smartphone or tablet and the device is lost, stolen or develops a fault so that the stored files are no longer available. An adequate backup practice might minimise the risk of this, but not everyone routinely backs up their device and many do not have the means to do so. The scope for data loss here seems to be considerable and HMRC needs to consider how it will deal with the issues flowing from that.

Question 8: Do you agree with the minimum transaction data fields proposed for trading businesses, including retailers? What other data fields might the record keeping software usefully include as a minimum?

77. Businesses are unlikely to want to be forced to do more than is strictly necessary during their transition to digital. However, businesses that are more technically advanced should not be prevented from transitioning fully should they so choose.

78. A VAT field will be an essential requirement for VAT registered businesses, but not for others.

79. It seems almost certain that retailers will need to input VAT figures manually, as well as gross takings, both to make sure that their VAT declarations are correct and also to exclude the VAT element of takings from “income”.

80. The move to digital seems to require significantly more information than that historically required from businesses for their taxation affairs. Although businesses would have their records, we do not see the justification for requiring taxpayers to enter every transaction they carry out nor for all record keeping to be done on a daily basis. Currently, a business may choose to upload the information into its accounts as a summary or make a bulk journal entry on a quarterly basis. There is a considerable difference between creating information digitally and simply keeping it digitally to make available at a later time.

81. At paragraph 3.11 of the consultation document it seems strange that basic information such as the customer/suppliers name is not considered necessary as part of the minimum information. Presumably the date would be the system date on the assumption that transactions are entered at the point of delivery on a mobile phone (hence daily), which is only likely to happen with the younger generation of users.

Question 9: Do you have any comments about reflecting the current VAT requirements in MTD-compatible software?

82. Some businesses complete monthly rather than quarterly VAT returns. It would be a considerable increase in the administrative burden if they were also required to submit monthly income tax returns under MTD. For example most small developers and builders would not wish to be put to the trouble of preparing monthly prepayments and accruals or work in progress valuations for MTD purposes simply because they wish to reclaim VAT (based upon invoices issued and or received) on a monthly basis.

83. We note from para 4.11 that the maximum threshold for the VAT cash accounting scheme will remain £1.35 million. This seems to imply that any software/app will need to cope with different thresholds for different purposes, an additional complication.

84. See also our comments to question 1.

Question 10: Do you have any comments on the additional data capture requirements for property income and capital gains?

85. Requiring taxpayers running a rental business to report income and expense details by specific property is more onerous than the current reporting requirements and also is more onerous than the rules applied to other businesses. This is an additional burden and one which appears to penalise honest taxpayers in order to provide information for HMRC’s risk assessment software. This seems unfair and is in direct contradiction to the first right of taxpayers in the HMRC Your Charter at para 1.1, ‘We’ll presume that you’re telling us the truth, unless we have good reason to think otherwise.’

86. Furthermore, this requires the business owner to constantly examine and decide how best to apportion expenses relating to more than one property, for example, direct expenses such as cleaning common areas and indirect expenses such as accountancy fees. This is not required for other business owners, or by the present law, which creates a single 'property letting business'. Landlords will frequently have a bulk insurance policy for all their properties, they may have a contract with a maintenance organisation that will do work on all the landlord's properties and issue a monthly invoice which may cover several properties. A requirement to split these out will be a burden that is of no benefit to the landlord.

87. Regarding capital gains, we would like to understand how HMRC intends to deal under MTD with connected party transactions undertaken at other than market value or which relate to assets located overseas.

Question 11: What should the minimum categorisation in the software be? Would additional sub-categories be useful?

Question 12: Do you have any comments on how businesses should reflect transactions and expenditure with non-deductible elements in the software?

88. The minimum requirement under the current self assessment rules allows 'three line accounts' by businesses with income below the VAT threshold and we see no justification for a change to this minimum requirement just because digital filing is introduced. What is important is that the business has the ability to support the income and tax allowable expenses if called upon to do so.

89. It is also difficult to see how pre-prescribed sub-categories can be useful given the variety of businesses that will be providing information.

90. If a business has adopted a system of expense analysis for management purposes, making them change that information purely to suit tax filing is an unwarranted additional expense.

91. In cases where a taxpayer's level of profit takes them outside the 'three line accounts' minimum disclosure, then the third party software developers should be encouraged to include within their software the ability to identify and adjust for private use, non-taxable income, and non-allowable expenses for the more common heads of expense and/or income categories, such as for motor expenses.

92. These paragraphs do not consider VAT. Ordinarily, a VAT registered business will be able to reclaim VAT so only the net cost will go into the tax estimate. However, VAT on some costs is not recoverable (eg, VAT on the purchase of cars available for private use) and VAT on most business entertainment expenses, or which is only partly recoverable, (eg, VAT on leased cars). The software/app will need to be able to allocate input VAT as deductible, not deductible and partly recoverable (eg, overhead input VAT that has to be apportioned using a partial exemption method of some kind).

Question 13: What prompts and nudges would be most useful to businesses?

93. Nudges and prompts are potentially an important part of MTD but there is a danger of 'overkill'. A common set should be developed but consideration given to them being tailored to be business specific. More use could perhaps be made of fixed rate expense deductions.

94. We are very concerned that changing the basis of assessment for unincorporated businesses at the same time as changing the process for filing and administering the system will lead to considerable confusion.

95. We would like reassurance that a taxpayer will not be considered to have been careless or negligent if it is later found that, having relied on a prompt or nudge, they make a mistake in their filing. Also if they were to 'override' a prompt they should also not be automatically considered to have been careless or negligent.

96. Prompts where current entries do not fit the profile of entries of earlier periods would be particularly useful.

97. We would be interested to know whether the ability for individual taxpayers to switch off prompts and nudges might be possible and if so, how HMRC would view the returns of a taxpayer who does this?

98. Common errors which members report that they correct for their clients include: personal and other disallowable expenditure, drawings of a sole trader being treated as a deduction and tax payments being treated as an allowable expense.

99. A particular area of difficulty for taxpayers is expenditure on property and the distinction between repairs and replacements which are revenue and those which are capital. We suggest that prompts and nudges be based on the guidance in the property toolkit.

Question 14: Do you agree that businesses should have the choice as to when to record accounting adjustments?

100. Businesses should be able to choose when to record accounting adjustments within the present filing and amendment time limits.

101. HMRC’s powers to make an enquiry should not start until the time for the taxpayer to make changes has expired. If they start earlier, the taxpayer should not be prevented from making a repair or amendment during an enquiry if the normal time limit for so doing has not expired.

102. It will not be possible to make adjustments for transactions in foreign currency until the average exchange rates for the year are known.

Question 15: Do you agree that business should have the flexibility to reflect reliefs and allowances when they choose?

103. We agree.

Question 16: What do you consider is the most appropriate approach to reflecting the effect of the personal allowance on an individual’s taxable business profit?

104. It should be possible to use personal allowances in a similar manner to the coding notice within the PAYE system, but with an ability for the taxpayer to override this should they so decide.

105. Where an individual has interests in more than one business, this could be more difficult, particularly where the businesses report to different quarters or where an interest in a partnership is involved.

Question 17: Is this the right treatment of partnerships? Are there any additional partnership issues that need to be considered?

106. An individual partner must be able to challenge the figure returned by the ‘responsible’ partner. This same basic principle should apply wherever a taxpayer has joint income or profit within their filing, or any other situation where HMRC seeks to ‘pre-populate’ a taxpayer’s account.

107. Large and complex partnerships need separate consideration and do not appear to have been catered for adequately in the design set out in this consultation, see our further comments to question 43.

Question 18: Is this the right treatment of individuals who receive income from property, let jointly?

108. It is not appropriate for a taxpayer's information to be updated by one of the other joint owners of the property, particularly if the only way to correct it is by asking the original filer of the information. Taxpayers must be able to challenge and/or provide their own provisional figure as an alternative. Joint reporting becomes impossible if some of the owners have opted for the cash basis and others have not.

Question 19: Is this the right treatment of subcontractors within the Construction Industry Scheme? Are there any other CIS issues that need to be considered?

109. We agree with this treatment, but as mentioned above, it should be open to the taxpayer to challenge the figure and/or provide their own provisional figure as an alternative.

Question 20: Do you have views on how detailed the summary data in the updates should be, and whether the level of summary data should be different depending on the size of the business?

110. Any move to MTD should not make the information requirement any greater than that presently set for self assessment.

111. Three line account information should be allowed for smaller businesses.

VAT

112. Paragraphs 5.13 and 5.14 seem to be suggesting that much more data would be collected through MTD than is collected on the current VAT return. This is counter to the trend towards less VAT data being returned on the regular returns and is counter to arguments advanced by HMRC and HM Treasury in relation to the EU's proposal for a common EU VAT return. This foundered because agreement could not be reached on the level of detail required, with the UK firmly in the "less is more" camp. It seems odd that having resisted a proposal that would have meant much more information being provided, HMRC is now bringing forward a proposal that seems to do just that.

Question 21: Do you have any comments on the categorisation of summary data in the updates?

113. Other than to re-iterate the general principle that MTD should not increase the amount of information required from a business, we have no comment to make on the categorisation of summary data to be included in the updates.

Question 22: Do you have any views on what VAT data the updates should contain? Do you have any views on the advantages or disadvantages of including VAT scheme data in the updates? If so, which schemes and which data should be included in the updates?

114. No further comment.

Question 23: What flexibility around update cycles would be useful?

115. The analysis within the consultation document does not address the complexities that arise for taxpayers who have multiple trades with different year ends or who have both a trade and a rental business. The quarter end will be chosen for business reasons, such as seasonality, in the first instance, rather than necessarily to coincide with reporting deadlines on other investments.

116. It seems sensible for businesses, where possible, to have contemporaneous VAT and MTD quarter dates.

117. Aligning quarter ends might not be possible where the taxpayer is a partner in one of the businesses for which reports need to be submitted.

Question 24: Do you agree businesses should be allowed one month to submit their update? Would any problems be caused for VAT registered businesses by standardising the time limit for updates for all taxes?

118. We regard the suggested 30 day time limit for uploading data as a minimum, but note that this would shorten the existing VAT filing deadline. We do not consider that the taxpayer should be required at the same time to make a declaration that all of the information is complete and correct given that it is unlikely that most businesses would make quarterly accounting adjustments for items such as accruals, prepayments or stock.

119. Some businesses could have difficulties meeting a 30 day time limit. For example, if bank statements are not received until later in the month following the quarter end or where suppliers invoices are delayed. For an agent with a large number of clients with the same year end, eg 31 March, this would create severe work flow problems. For that reason we suggest a six week deadline rather than merely keeping the existing extended VAT deadline of seven days after the month end, which would provide businesses and their agents with a little extra flexibility. This would also help with staff absences for illness, holidays, etc.

120. A single due date for both MTD updates and VAT information would be simplest for some businesses but, for larger ones in particular, it does mean that accounts staff will need to deal with both at the same time. While for the very simplest businesses, that may be little, if any, additional burden, for others combining the two will run the risk of overburdening staff, leading potentially to more errors, especially if management accounts preparation is on the same cycle. Although some businesses choose to align direct tax and VAT periods of account, others offset them in order to smooth the workload.

121. We note that although most VAT registered businesses have one month and seven days after the end of the VAT accounting period to file a return and make any payment due, large businesses have just one month to file a quarterly return and must make two payments on account, during the accounting period, followed by a balancing payment. The MTD provisions for large income tax paying businesses, such as partnerships, have not been considered adequately in the MTD design.

122. Retaining flexibility seems to be the solution.

Question 25: What method of deriving a business's start date for providing updates under Making Tax Digital would be most straightforward for businesses?

123. The majority of our members favour Option 1 as set out in the consultation document particularly as it does not duplicate the reporting of data that will already have been sent to HMRC within the 2018/19 tax return.

124. The wording in the consultation document is unclear. Paragraph 5.29 states that the business update cycle would begin on the first day after their first accounting date that follows 5 April 2018. For a business with a 5 April year end the first date after their accounting date that follows 5 April 2018 is 6 April 2019. This interpretation is contradicted by paragraph 5.31.

125. We are however extremely concerned that there appears to be no specific provision for the date by which a new businesses starting after MTD is in place must notify HMRC that it is trading. Currently, this would be 5 October following the end of the tax year, although in practical terms will be the following 31 January. Unless specific provision is made, a new business would now need to make its first MTD return just four months after starting to trade.

This would be impractical for many – especially as it will not always be obvious what was the start date of the business.

Question 26: Do you wish to make any comments about the operation of 'in-year' amendments to updates for the purposes of profits taxes or VAT?

126. It should be as easy as possible to make 'in-year' adjustments for all taxes and there should little or no risk of penalties as a result of making such adjustments.

127. We suggest that it should be the norm to include any adjustments in the next available quarterly upload and for any final adjustment of unresolved matters to be included in any final annual declaration, the time limit for which be aligned with the existing time limit for filing a self assessment tax return.

Question 27: Do you agree that the process of finalising the regular updates should be separate to the regular updates?

128. Yes, this should be ten months after the year end in line with the existing time limit for filing a self assessment tax return. The present facility to amend or repair a self assessment return up to one year after the filing date should apply also for the information submitted under MTD.

Question 28: Do you agree that businesses should have nine months to complete any End of Year activity?

129. We suggest the time limit for completing any end of year activity should be ten months, so 31 January, after the end of the year. There was a suggestion of bringing this deadline forward to 30 November several years ago, but the government decided not to pursue this when it became clear that considerable amounts of information was of necessity only received by agents much later in the year than they had appreciated. The consequences of bringing the deadline forward would have been that estimated figures would have been needed and a large number of returns would need to be resubmitted.

130. Certainly in the short term, we advise against introducing a nine month deadline which would actually impose an unwelcome Christmas/New Year tax deadline for 31 March year ends.

Question 29: What criteria should be applied in determining whether to exempt a particular business or business type from the requirements of MTD?

131. There are two elements to MTD: digital record keeping and filing digital quarterly returns. These impose different challenges and we consider that they need to be considered separately.

132. In designing and then implementing MTD, government should decouple the digitalisation of record keeping from any quarterly reporting requirement. While in time it should be possible with the right software and skills to ensure that the two functions can be made seamless, a more gradual implementation may be easier to achieve for those whose business administration skills would not easily adapt to embrace an end-to-end mobile phone App or IT system.

133. The current timetable for implementing MTD is unrealistic. While we support the move to digital, it will take at least five years and possibly up to ten years to do this properly. Learning lessons from previous large IT projects suggests that rushing implementation leads to problems both for HMRC and for users, whereas a controlled roll-out stands a much better chance of success.

134. If digital record keeping is believed to be the answer to closing the tax gap, then encouraging more businesses first to move to a more systematic approach to record keeping could be the first step. A Chartered Accountant would already help his or her client to do this, teaching them to use a spreadsheet for example, when the client is able to do so. Even where paper records are maintained (monthly expenses in a file or even a carrier bag), this is a system which may actually be perfectly satisfactory for that business.

135. If earlier reporting is the primary issue, then enable agents to file quarterly reports of income and expenses on behalf of their clients from the outset, but allow them to do so from records they have compiled (eg, excel spreadsheets). This is of course much like the current process for VAT returns.

136. The two main concerns reported by our members are the disproportionate cost to the business and the impracticability After extensive consultation, we have concluded that we cannot consider supporting mandation at this time: there are too many situations where the requirements of MTD make it impossible for taxpayers to comply. This should instead be a voluntary system for a period of at least five years from when a fully functioning MTD system is in place.

137. In addition to the lack of broadband, other cases where an exclusion would be necessary regardless of when it is introduced, are:

- Individuals with more than one business interest. MTD will be particularly difficult where the businesses have different quarters and it is impossible to align them
- Individuals with sole as well as shared business interests. For example in a partnership, not all of the partners would find their personal business quarters align with those of the partnership
- Individuals with personal difficulties involving literacy or numeracy
- Lloyd’s underwriters profits and losses are reported three years in arrears whereas income from funds at Lloyds are reported for the year ended in the tax year so it is difficult to understand how this can be reported digitally in real time. As dividends and interest on the funds at Lloyds are part of the profit the digital reporting tool will need to have the capability of reporting dividend income. There will also be difficulties in reporting transactions in foreign currencies and accounting for forex gains and losses. As there are only about 290 individual members and about 700 LLPs it seems a waste of resources to adapt MTD to fit such a small group.
- Not all Members of Parliament and members of the Judiciary are currently able to file tax returns online for security reasons and may also need to be excluded from MTD

138. Cost disproportionate to the size of the business or type of business should be a key feature of the exemption from MTD. This is difficult to frame in legislation and we have therefore suggested that businesses with income below the current VAT threshold should be exempt.

139. Consideration also needs to be given to overseas businesses that operate in the UK through a branch and have a permanent establishment. If all their accounting is recorded in their home country, it is unclear how MTD could operate.

140. Some overseas businesses have only VAT compliance obligations in the UK. It would seem sensible to exclude them from the full rigours of the MTD obligations while leaving their VAT obligations intact.

141. Consideration should also be given to non-resident landlords whose only UK taxable income is the income from their UK property. Many such landlords do not have a liability to UK tax because of the availability of the personal allowance. It does not seem sensible to require quarterly reports where is clear that a liability to UK tax is unlikely. In this regard, consideration should be given to how the Non Residents landlord Scheme should operate under MTD.

Question 30: Should charities be exempt from the requirements to maintain digital records and to update HMRC at least quarterly?

142. Our members agree that it is reasonable for charities to be exempt from the requirements to maintain digital records and to update HMRC quarterly.

143. If charities have no taxable income, quarterly reporting would be a meaningless imposition. However, the same is equally true of many other small businesses which make little or no profit, particularly in their early years. For these businesses, imposing digital record keeping and reporting will be a disproportionate and distracting obligation at a time when they are most vulnerable. Such businesses gain most by keeping a close regular watch on their cash flow.

Question 31: Should trading subsidiaries of charities be exempt from the requirement to maintain digital records and to update HMRC at least quarterly?

144. Corporate trading subsidiaries of charities that have undertaken to gift aid the whole of their profits to the charity should be exempt from the requirement to maintain digital records and to update HMRC quarterly. In such cases, MTD may still be adopted voluntarily, but would do so if it was of benefit of business rather than to save the costs of HMRC since there will be no taxable profits. VAT reporting may still be required.

Question 32: Should CASCs be exempt from the requirement to maintain digital records and to update HMRC at least quarterly?

145. See our response to question 30 above. Our members also believe that a similar exemption should be available to all clubs, societies and businesses such as flat management businesses that are only taxed on investment income.

Question 33: Should businesses within the insolvency process be included within the scope of the requirement to maintain digital records and to update HMRC at least quarterly; and are any special arrangements required for this group?

146. Businesses in the process of insolvency will each have different circumstances. MTD should be optional for this group.

Question 34: Which businesses should be included within a consistent definition of persons ‘unable to engage digitally’?

147. It is the circumstances of the individual taxpayer which are most likely to determine whether a business is able to engage digitally or not, see comments to question 29.

148. The corporation tax, PAYE and VAT regimes do indeed take different approaches in defining those who cannot engage digitally, para 7.20, but these taxes have different requirements. A straightforward small unincorporated business run by a sole individual is unlikely to have any mandatory digital obligation at all until income reaches the VAT threshold. At that point, the requirement is still minimal compared to what is now being proposed under MTD.

149. There is a fine line between being ‘unable to engage digitally’ and being ‘able to if you try very hard and spend a long time doing it and in doing so incur disproportionate cost’. In either case, mandation is bad for business and we are very concerned that those who suppress sales in an analogue world will continue to try and do so in a digital world.

150. We do not consider that HMRC has sufficient staff or funding to be able to undertake a sufficiently intense training programme before 2018, so as to be able to reduce the number of individuals as could be managed within a consistent definition of persons ‘unable to engage digitally’ built on current legislation.

151. If the VAT registration limit is used as the level at which MTD becomes compulsory, the business population affected will fall significantly, leaving a more manageable population in need of assistance.

152. In addition, there should be a general exemption for Universal Credit claimants, at least until such time as when the obligation to report quarterly can be met by an information feed from DWP to HMRC.

153. The definition here is crucial. Although this question is couched in terms of businesses, the comment at paragraph 7.21 of the consultation document is a helpful starting point. Friends and family members, professional deputies (likely to be solicitors or Chartered Accountants) or members of the professional deputies panel of the Office of the Public Guardian may be appointed by the Court of Protection in the case of personal taxpayers who are mentally incapable of handling their own affairs. Clearly in such cases the taxpayer is unable to engage digitally, but the question that arises is whether the question of the ability to engage will depend on the status of the taxpayer or of the deputy.

154. A similar issue arises in the case of taxpayers where an enduring power of attorney has been registered as a result of the taxpayer losing capacity. Presumably taxpayers who have executed an enduring power of attorney which has not been registered, will be deemed to be able to engage digitally, or will a mental capacity assessment be required.

155. Matters are more complicated in the case of taxpayers who have executed a lasting power of attorney. This has to be registered to be effective, but registration does not mean that the taxpayer is unable to engage digitally as he or she is not necessarily incapable of handling their affairs. Who is to determine whether the taxpayer is able to digitally engage or not? Again will a mental capacity assessment be required?

156. The issue also arises in the case of taxpayers who are resident in care or nursing homes who have nobody available to help them. We assume that such people will be deemed to be persons who are unable to engage digitally.

157. Does HMRC envisage all executors and trustees being subject to MTD? Will they be deemed to be running businesses? Would the position be different depending on whether private individuals or professionals such as solicitors or Chartered Accountants were acting as the executors or trustees?

158. Many taxpayers who are themselves unable to engage digitally do interact digitally with HMRC because they engage an agent. This is a further reason why agents must be able to undertake all transactions on behalf of their clients, including bookkeeping.

159. Establishing a satisfactory definition of those unable to engage digitally is necessary but consideration also needs to be given to how HMRC will identify those who fall within that definition. There is the potential for this to develop into a very cumbersome approval process for both the taxpayer and HMRC. We recommend a light touch approach – it might be best to start with a self-certification approach.

160. Individuals who are able to engage digitally may become unable to do so as a result of disability, age or because they can no longer afford the necessary equipment. Variable conditions can mean that taxpayers are able to engage digitally at some times but not at others and they may move between the two groups at frequent intervals.

Question 35: Do you agree that £10,000 annual income is an appropriate threshold for exempting businesses from Making Tax Digital? Do you have any other comments on how the exemption should operate?

161. The proposed exemption of £10,000 turnover is too low. At this level, the business will not be paying tax even if it applied to taxable profit. As an absolute minimum, the exemption would need to be set such that tax would be due on profits. We understand that this limit is suggested by HMRC in order to assist with its compliance activities, but MTD begins with a change to fundamental accounting techniques. It offers the UK an opportunity to think carefully about fundamental principles of financial and tax reporting. Accounts are not only used for tax and we should not seek to change the rules just to accommodate MTD, but instead should consider whether change is appropriate in a wider context.

162. For this reason, MTD should not be mandatory. Any exemption threshold should be set at an amount which is no less than the VAT registration limit.

Question 36: Should the smallest unincorporated businesses that are not exempt have an extra year to prepare for Making Tax Digital? How should eligibility for this group be defined?

163. We consider the timetable for implementing MTD to be far too ambitious. The various elements should be implemented piecemeal while the IT is still being implemented and tested. None of this should be mandated.

Question 37: Do you agree that the principles set out in Fig. 7.3 are the right ones to use in determining eligibility for an exemption? Are there any additional principles which should apply?

164. While previous results will provide an indication of whether a business will be eligible for an exemption, this could not be the immediately prior period. It would instead need to be based on the results of the last accounting period ending 12 months before the start of the current year.

165. For example, if the results for the year ended 31 March 2022 were the first to exceed the MTD exemption limit, that period’s end of year activity report would not be needed until nine months later, see para 6.17, so 31 December 2022. It would be unreasonable for the business to switch to digital, and so MTD, from 1 April 2022.

166. We consider that MTD should not be mandated, but even if it becomes compulsory for businesses with income above the VAT threshold, it should be voluntary during the first two years of the life of a new business. New businesses do not immediately consider tax when they start trading and their first decisions should be around creating a successful and sustainable business rather than immediately choosing MTD software.

Question 38: Which additional groups (if any) should be exempt from the requirements to maintain digital records and to update HMRC at least quarterly?

167. Many taxpayers may feel more comfortable with an old style manual ledger from which they could enter quarterly figures by some sort of interface. In particular there may be businesses coming to the end of their economic life eg, the proprietor retiring, and it would be unreasonable to put them to the possibly high cost of transition for what may only be one or two years of filing. There is a very real possibility that many older people may decide to just retire earlier than they had planned because they feel the cost, stress and effort needed to move to digital, just isn’t worth it. This would be a loss to the UK economy. We have had several representations from older members saying just this.

168. For the reasons stated above, deputies, attorneys, executors and trustees should be exempt from the MTD requirements with the proviso that there would be nothing to stop them doing so if appropriate.

169. See also responses to question 32 above.

Question 39: Do you believe that there is the opportunity for MTD to create savings for your business? What percentage time reductions would you see from the following?

a) Targeted software tax guidance (prompts and nudges to get information right first time).

b) Gathering, collating and inputting data.

c) Reporting obligations through providing regular updates.

d) Any other potential savings not covered above.

170. We are unable to think of any instance where MTD would result in savings for business, either monetary or through saving time.

a) These are unlikely to lead to savings and indeed may slow the bookkeeping process down for some who do not understand the guidance being offered. Ongoing training as tax rules and software change will lead to more time spent on administration.
b) Businesses already gather, collate and input data so there is unlikely to be any saving from MTD in this area.
c) The regular reporting requirements under MTD are an extra burden on business rather than a saving.
d) No savings were identified.

171. If businesses thought they would benefit from digital record keeping they would do so voluntarily. If compulsion is required to make it happen, there must be a burden. We consider that there will be additional costs for business both on implementation and also ongoing.

Question 40: Do you think there are different business sectors or sizes likely to benefit more from MTD? If so, what would these be?

172. We could not identify any business sectors or sizes likely to benefit more from mandatory MTD. Businesses that are already committed to digital record keeping could possibly benefit, but they would have moved to or continued with digital records in any event and so the move to MTD will mean simply that they have to report quarterly whereas presently they only have to report annually.

Question 41: What costs might you expect your business to incur in moving to the new regime? Please provide details of the costs for:

a) Time spent in your business familiarising with the new processes and conversion to these new processes.

b) Software expenditure costs (new or upgrading software).

c) Hardware expenditure costs (purchase of a computer, tablet device, etc).

d) Any other costs which are not covered above.

173. We have been able to identify the following general points:

a) The costs to transition are likely to vary depending upon the size and complexity of the business concerned and the present state of the record keeping;
b) The costs of software will also vary depending upon whether the present records of the business are manual or digital. These could be kept to a minimum if businesses were permitted to retain their current record keeping with a requirement to digitally upload their manuscript/spreadsheet information on a quarterly basis.
c) The costs of hardware could be substantial for those businesses that are presently not using IT whereas they may be minimal for those who are IT literate.
d) A number of businesses are likely to incur outsourcing costs as they will prefer to continue to use a professional to keep their records up to date digitally. If an agent has to file four additional returns each year, costs will inevitably increase as even if there are to be no checks or penalties attached, professional responsibility will mean they need to be checked.

Question 42: Do you expect that your business will incur additional on-going costs as a result of these changes? Please provide the details of the additional costs or time for:

a) Additional support from your accountant or tax agent.

b) Additional time spent gathering, collating and inputting data.

c) Additional time reporting obligations through providing regular updates and any end of year activity.

d) Any other costs or time spent not covered above.

174. Yes, there will be ongoing additional costs:

a) It is anticipated that there will be a cost for additional support from agents
b) There would be no extra cost for gathering, collating and inputting data provided taxpayers can retain their present records from which they can upload a summary each quarter
c) There will be additional time in reporting as there will be a quarterly reporting obligation rather than annual. This is most clearly seen when one looks at a property rental business
d) It is likely that many smaller businesses will comply by out sourcing their record keeping in the future
e) There will be additional costs for agents who may need to buy various software packages in order to receive information from their clients. The alternative would be manual entry onto the agents own software which would cost time and therefore money.

Question 43: Will particular businesses (e.g. partnerships) experience more difficulty in adapting to the changes? If so, please provide details, including any additional oneoff costs or ongoing costs.

175. In addition to partnerships, other businesses which will experience difficulty adapting to MTD are farmers, property businesses, seasonal businesses and businesses such as those involved in building and construction where they have high values of work in progress or fast fluctuating levels of stock or debtors/creditors. If these are only adjusted annually, any tax calculation based upon the quarterly submissions will be meaningless, and businesses should be warned not to rely on them to accurately predict their tax liabilities.

Partnerships

176. By their nature, partnerships will usually have more than one individual interested in their profitability. Consequently, most partnerships need timely accounting records. Larger partnerships in particular, have sophisticated mechanisms. Tax reserves are held to ensure that tax can be paid when it falls due. Quarterly reporting would not assist this process, but would merely add cost.

177. A start date of 2018 is not possible for many simple income tax paying businesses and certainly not for larger and more complex partnerships.

178. Many partnerships do not know during the year how profits will be finally allocated at the year end. Quarterly filings will have to be made based on estimated profit sharing ratios and the final allocations between partners will inevitably be different. Numbers could change for a variety of reasons such as:

- In so called ‘Eat what you kill firms’, decisions about how profits are divided are often not made until after the year end
- In Lockstep firms, valve arrangements mean that in some years a partner group will receive a profit share and in others they will not
- Multinational firms will need to incorporate changes in foreign exchange rates when allocating profit shares
- In all firms, special profit sharing rules will be used to allocate profit shares to leavers and joiners.

179. Allocating quarterly figures to a partners’ tax account would be problematic from a firm’s management perspective. Even with disclaimers, it will raise the expectation of a particular profit share. If the actual profit share is different there are likely to be more discussions than would otherwise be the case.

180. In addition, partners may make incorrect decisions, eg, making pension payments, based on the partner's tax account numbers which are later adjusted.

181. We are expecting a further consultation from HMRC dealing with MTD for complex businesses, which includes large partnerships. It is to be hoped that there will be exceptions from the MTD rules.

Question 44: If you are an agent, please provide details of how these changes will impact on your own business, including details of any one-off and ongoing costs or savings. How do you perceive that these changes might affect your clients?

182. Many of our members are agents. The most likely impact on their own businesses will be the need to invest in and become more familiar with a greater number of software packages in order to help clients fulfil their reporting obligations.

183. Time will tell whether MTD will reduce the general skill level within the offices of local Chartered Accountants. Experiences of introducing other recent major software changes has certainly not led to an immediate de-skilling of staff since the complexity of the tax system still seems to need considerable human intervention to arrive at the correct amount of tax due.

184. The extra work on MTD is likely to be low margin and clients may not be prepared to pay extra for the service as they will see no benefit from it. The additional time required may result in the practitioner reducing the size of their client base or clients deciding to go it alone. There is therefore a danger than many clients may be cut-off from receiving the advice they need and consequently that tax compliance will fall rather than improve.

APPENDIX 1

ICAEW 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 via http://www.icaew.com/en/about-icaew/what-we-do/technical-releases/tax).

APPENDIX 2

ICAEW SUMMARY OF SURVEY RESULTS (MARCH 2016)

Just a quarter of businesses surveyed say they manage their accounts electronically using accounting software (25%)

- The same proportion say they use a solely paper-based system (25%). The remainder are either using electronic (non-software based) methods or else a mix of these and paper-based management. A minority of those surveyed did not know what method was used.

Maintain your accounts electronically using accounting software	25%
Maintain them electronically (e.g. using MS Excel) but not through any specific accounting software	19%
Maintain them using a mix of electronic and paper-based systems but not through any specific accounting software	26%
Maintain them using a paper-based system rather than electronic or specific accounting software systems	25%
Don't know	*6%*

Overall results for all businesses surveyed (500)

- Looking at the results broken down by size of business we can see that medium and large businesses are much more likely to manage accounts electronically using accounting software (89% and 81% respectively) whilst sole traders and micro-sized businesses are much more likely to use paper-based, or a mix of paper-based and electronic systems (e.g. MS Excel) rather than any accounting software.

The majority of businesses surveyed used an external accountant to prepare and submit their last tax return (71%)

- The smallest businesses (sole traders & micros) were more likely to use an external accountant, whilst this becomes less common.

Using an external accountant	71%
In-house/ by you	14%
Using someone else outside the business (e.g. friend, family, contact)	8%
Don't know	*7%*

Overall results for all businesses surveyed (500)

Over three-quarters of businesses surveyed said their last tax return to HMRC was submitted online (77%) with just under a fifth saying they submitted a paper return via post (17%)

Online	77%
Paper via post	17%
Don't know	*6%*

Overall results for all businesses surveyed (500)

A third of businesses said they were paying between £601- £1,000 to their accountants to prepare and file their annual accounts and tax return with HMRC (33%)

- When looking at the results broken down by size of business, we can see that sole traders are more commonly paying between £600-£1,000 (39%) whilst all other businesses, from micro up to large, were more likely to be paying £1,500+.

Under £300	5%
£301-£600	19%
£601- £1,000	33%
£1,001- £1,500	7%
£1,500+	17%
No specific charge made for this	1%
Don't know	*18%*

Overall results for all businesses surveyed (500)

Over half of businesses surveyed stated that they supported HMRC's stance of encouraging businesses to send in their information online (55%)

- Whilst only 14% of businesses opposed this, just over a quarter were indifferent (28%)

Support	55%
Oppose	14%
Indifferent	28%
Don't know	3%

Overall results for all businesses surveyed (500)

Whilst HMRC's stance is broadly supported, businesses are clear that online information filing should not be made compulsory, with just under three-quarters stating so (72%)

Compulsory	18%
Not compulsory	72%
Don't know	10%

Overall results for all businesses surveyed (500)

Note on this research (to be provided with any public/media release)

- *Data drawn from market research conducted via telephone with a representative sample of 500 businesses across the UK (data weighted accordingly to reflect UK business population). Fieldwork took place between 15th - 26th February, 2016. Research undertaken by IFF Research on behalf of ICAEW. This survey adheres to the Market Research Society code of conduct.*