HMRC
100 Parliament Street
Westminster
London SW1A 2BQ
By email: businessprofits.admin@hmrc.gov.uk

31 August 2021

Dear Sirs,

**BVCA response to the HMRC consultation on basis period reform**

We are writing on behalf of the British Private Equity and Venture Capital Association ("BVCA"), which is the industry body and public policy advocate for the private equity and venture capital ("PE/VC") industry in the UK. With a membership of over 700 firms, we represent the vast majority of all UK based private equity and venture capital firms, as well as their professional advisers and investors. Between 2015 and 2019, BVCA members invested over £43bn into nearly 3,230 UK businesses, in sectors across the UK economy ranging from heavy infrastructure to emerging technology. Companies backed by private equity and venture capital currently employ 972,000 people in the UK and the majority of the businesses our members invest in are small and medium-sized businesses.

We are grateful for being given the opportunity to provide feedback on the consultation document and we look forward to discussing our comments with you.

*Timing and rationale*

While we can see the attraction of aligning basis periods with tax years for certain partnership (and LLP) structured businesses, we also think, as discussed below, that it will raise significant issues for others. Accordingly, we are concerned that the legislation is in danger of being rushed, with a short timeline for the consultation, and we would therefore suggest that additional discussions are entered into involving affected groups, including the BVCA.

The large number of businesses potentially adversely affected by these proposals renders it important that they are considered very carefully and that any legislation is the product of appropriate engagement with interested parties.

We note that the consultation document (the "Consultation") published with the draft legislation on 20 July 2021, suggests that those who find the existing basis period system difficult are sole traders and small partnerships. Larger businesses have specifically advised that the rules are straightforward (or easily manageable) for them (see the Executive Summary of the Consultation) and therefore, we do think there is a question of whether this proposed change does in fact represent a simplification, which is the intended objective of the reform. In addition, we are unsure whether the other stated objective of reform, to prepare businesses for MTD, is in fact applicable to many businesses which are established as LLPs as we understand that HMRC have confirmed that LLPs are excluded from the first phase of MTD. Thus, we are unclear whether the reform of income tax basis periods is really a pressing need where businesses are established as LLPs given the period for MTD applying to them is as yet uncertain and undefined.

Accordingly, we would suggest that due consideration is given to delaying this reform to ensure that it is accorded sufficient comment and consultation with impacted parties.

*Key comments*

Before discussing some details of the proposals, we would note that our concerns relate principally to two areas relevant to UK businesses (investment managers and advisers) which are part of larger, international organisations, often headquartered in the United States. Our main concerns are:

(a) these UK businesses are often not free to select their own accounting period year end without impacting the wider, international business, and, in those cases, the proposals will lead to significant administrative and operational complexities and costs; and
(b) the way in which double tax credit rules work in the UK and other jurisdictions (for instance, the United States) mean that misalignment of the period for which UK and non-UK taxes are paid can give rise to significant complexity and unrelievable double taxation.

Noting these potential issues with the proposals, discussed in more detail below, a general suggestion we would make is that, since many businesses have noted that they do not find the current rules difficult, would it not be appropriate to operate a dual system so that taxpayers can choose the least burdensome option for them? This would appear to achieve the aim of simplicity, since businesses could choose what is simplest for them. If this cannot be accommodated, then, perhaps consideration could be given to the introduction of specific rules meaning that those with a December 31 year end date can retain that basis period end date as discussed further below.

*Specific points*

Many of the affected fund manager LLPs are established as part of international operations, frequently headed by a parent located in a jurisdiction with a December 31 tax year end (often in the United States but also in other European or Asian jurisdictions). Accordingly, as identified at paragraph 3.11 of the Consultation, it will not be practical for these businesses to change their year end. If they were to seek to change their year end this would be likely to lead to material administrative (and possibly other) consequences for the rest of their group as there would be misalignment of profit calculations between the UK business and non-UK business that would need managing. International management would need convincing that changing the UK year end was worth this extra burden and would also add to the list of complexities associated with their UK operations. Thus, the ongoing burden on the wider business (and UK) would be undesirable. The proposal that the UK business might be required to file an amended return each year if the international business year end was close enough to April that the UK business would not have final figures to prepare its tax accounts is, we think, administratively burdensome. In principle it does not seem right that a business should fill in its tax return on an estimated basis and businesses would need clear reassurance that doing this in good faith would not expose them to any kind of penalty.

Of the alternative options given in the Consultation, the most appropriate would be to allow for final figures to be included in the subsequent tax return. However, this does not deal with wider

complexities which can arise to LLPs affected in this way. This issue alone supports the suggestion above, that the proposed reforms should be optional for businesses.

Another example of further international complexity arises in relation to potential foreign tax reliefs. Any lack of alignment between the timing of tax payments in the UK and another relevant jurisdiction may result in difficulties navigating available credits. HMRC will be well aware from other discussions how US citizens working in the UK will be subject to both US and UK tax on their remuneration and that there can be complexities around ensuring full double tax relief can be claimed. As a first hurdle, it is unclear how foreign tax credits would be treated over the five year transition where there might be significant timing differences between payment of UK and non-UK tax. Furthermore, in calculating profits of certain LLPs with US links, reliance will be placed on the US Form "K1" of underlying partnerships which is based on the US tax year which ends on December 31. This, and potential non-US equivalents, may have to be revisited in the context of the change of basis periods from accounting period to tax year. A similar issue may also arise in relation to a non-UK business e.g. an individual who works for the UK sub-advisor to a US fund manager, and who (in addition to any UK remuneration) has an interest in the US manager thus receives a form K1. It is not wholly clear how the legislation is intended to work in these circumstances.

We would urge further discussion on these areas since they are very complicated and any risk that the proposals might lead to unrelievable double tax would obviously be a serious impediment to individuals subject to tax in the UK and elsewhere continuing to work in the UK.

We also note that there may be differences between partners' positions which impact the desirability or otherwise of the five year profit spreading versus acceleration. It will be difficult for partnerships to manage the diverse interests of partners in this regard. We also note that, in the case of accelerated payment, there is the potential for permanent loss of overlap relief and we consider it to be desirable and fair for there to be greater flexibility on that point, e.g. by allowing individuals the option to carry back any unrelievable overlap relief in the year of transition further (in line with the normal termination rules) or to be carried forward.

In terms of other areas possibly affected by these reforms, we would draw your attention to the salaried member rules relating to LLPs. These rely heavily on the application of certain tests of profits arising during a period of account and currently this is carried out in relation to accounting periods. No explicit consideration appears to have been given to these rules although we think that it might well be the case that they would not impact because the proposals are simply deeming an additional period's profits arising in the tax year 2022-23 for tax purposes rather than deeming an actual payment to be made. This sort of issue would, however, need to be addressed in either the legislation or clearly in contemporaneous guidance. The possibility of these and other similar issues simply highlights, however, our main point that if these proposals are to be pursued then further time should be given to considering all possible implications.

*Conclusions*

Overall, we are concerned that proposals designed to simplify may create undue complexity for our members established as LLPs at a time when HMRC are seeking to attract investment managers and their funds to the UK through the use of the new asset holding company regime and similar measures. Great care should thus be taken and, since some of these issues are complicated, especially in an international context, we should welcome a specific meeting with HMRC.

We would be grateful for an opportunity to meet and discuss the feedback provided in this letter. Please let us know if you have any comments or questions in the meanwhile.

Yours faithfully,

Mark Baldwin
Chairman of the BVCA Taxation Committee

BVCA

## Detailed feedback on consultation questions

**Question 1: Do you think that the proposed 'tax year basis' for trading income is the best option for simplifying the basis period rules, and the best way to achieve simplicity and fairness between businesses? If not, do you think there is a better option?**

No, not necessarily. As noted above, since many businesses have noted that they find the existing system straightforward and many others will be adversely affected by the changes and unable to alter their accounting period to mitigate the effects, it would seem fairer (and more straightforward) to allow businesses to choose between the two methods. Those who find the current system complicated may make the change and those for whom the use of the current model is operationally manageable and understood (notably those within large international organisations) may retain the existing system. This would seem to be consistent with the HMRC objective of simplicity in that businesses may choose whichever is simplest for them. It also should make no difference to the exchequer since this change has not been identified as raising revenue and if bringing forward the collection of tax is an objective, then other methods could be considered (e.g. considering the timing of payments on account for example).

**Question 2: Will the proposed tax year basis have an effect on how businesses choose their accounting date, and whether they choose 31 March or 5 April?**

As noted above, many businesses will not be able to change their accounting date owing to wider, potentially international, operations.

**Question 3: For businesses with a non-tax year accounting date, what would be the cost of the additional administrative burden of apportioning profits into tax years? Are there any simpler alternative approaches to apportionment?**

Again, as noted above, the administrative burden here would be significant in calculating not only profits but also available credits, impact on foreign taxes etc. An option to retain an accounting year basis would resolve this. In any event, the idea of amended returns is likely to be burdensome and the use of the subsequent tax year returns would seem to be more appropriate.

**Question 4a: Businesses with accounting dates later in the tax year will have to estimate profits for a proportion of the tax year, before accounts are prepared. For which accounting dates do you think this would be necessary? Do you expect that businesses that have accounting dates earlier in the tax year than 30 September will have to estimate profits? If so, which types of business would be affected?**

Exactly what year end date will create an issue will depend on the reporting processes of each relevant business and we do not think that a cut off date could sensibly be applied. However, as stated above, we think that the most common accounting date for investment management/advisory LLPs will be December 31, and businesses with that date would certainly have issues.

**Question 4b: Will estimation be a significant burden for those businesses affected, and what will the cost be? Are there any simpler alternative methods of estimating profit or finalising estimates, which could mitigate any extra administrative burden?**

See above.

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**Question 5: Would the proposed equivalence of 31 March to 5 April help businesses that would have to make apportionments to work out their profit or loss under the tax year basis? Would extending this equivalence to property income help property businesses, which would otherwise have to apportion profit or loss each year? Are there any problems with this equivalence proposal?**

No specific comment.

**Question 6: Are there any specific issues, costs, or benefits to the tax year basis for partners in trading partnerships?**

No specific comment.

**Question 7: Are there any other issues and interactions to consider for the tax year basis, or the transition, in the areas of tax outlined in paragraph 3.33?**

No specific comment.

**Question 8a: Does the proposed method of transitioning to the tax year basis using a long basis period combined with allowing all unused overlap relief achieve the best balance between simplicity and fairness? If not, is there a better option for transition?**

As stated above, there are issues with the use of overlap relief including in the international context and in the context of potential absolute loss of overlap relief.

**Question 8b: Are there any other specific circumstances on transition to the tax year basis that would require additional rules?**

We think that the possibility that there are warrants much more consideration of the proposals over a longer time period.

**Question 9a: Would the proposals for spreading excess profit mitigate the impact of transition without affecting the simplification of moving to the tax year basis? If not, are there any other ways of mitigating the transition impact that you would suggest?**

This is a difficult area and might be best resolved by retaining the option of choosing to continue to use the accounting period basis.

**Question 9b: Would the proposal to spread excess transitional profits over five years be enough to resolve the cash flow impacts of the proposed reform? Are there any situations which would need additional rules or anti-avoidance provisions?**

No specific comment.

**Question 10: Are there any other impacts, benefits, or costs in the core policy, transition, or mitigation proposals that we have not considered above?**

No further specific comment in addition to the above although, as we say, the general concern is that the proposals are being rushed, do not represent a simplification for many LLPs and that careful consideration needs to be given to all potential issues that the new rules would raise.