

Amendments 14 to 17 to Schedule 1: Abolition of basis periods

Summary

1. These amendments are to Schedule 1 to Finance (No 2) Bill. They adjust the ordering of steps in the taxation of transition profits. This ensures tax reducing reliefs can apply in full, while maintaining the separation of transition profits from the profits otherwise arising in the tax year.

Details of the amendments

2. Paragraph 75 determines the liability to income tax on the transition profits chargeable to income tax in a tax year, with reference to the Steps in the calculation in section 23 of Income Tax Act 2007. The amount of the transition profits chargeable, reduced by any reliefs set against them at Step 2, is left out of the calculation at Step 2. The difference between the tax liability calculated at Step 5, and the tax liability that would have been calculated at Step 5 if the amount left out at Step 2 had not been left out, is then added at Step 7.
3. Amendments 14 and 15 amend subparagraphs 75(2)(a) and (b) to define the amount chargeable as the “transition component”.
4. Amendment 16 amends subparagraph 75(2)(b) and replaces subparagraph 75(2)(c) to separate the deeming conditions relating to Step 2 and net income. The amendment also introduces new subparagraph 75(2)(d) which provides for the difference between the tax liabilities calculated at Step 5 under subparagraph 75(3) to be treated as an amount of tax calculated at Step 4, instead of being added at Step 7. This has the effect of allowing tax reductions, applied at Step 6, to be deducted from the tax charged on the transition profits.
5. Amendment 17 replaces subparagraph 75(3) to clarify how the difference between the tax liabilities calculated at Step 5 is determined, in particular that the amount treated as an amount of tax calculated at Step 4 is to be ignored for this purpose.

Background note

6. Clause 7 and Schedule 1 change the basis of taxation for trades, professions and vocations from the current year basis to the tax year basis, for the tax year 2024-25 onwards, with a transition year in 2023-24 to tax profits which would otherwise escape taxation and to give relief for profits taxed twice (overlap profit).
7. This has been introduced to simplify traders’ reporting responsibilities and remove

complex rules relating to basis periods and overlap profit. It also promotes fairness by taxing traders closer to the point at which their profits are generated, removing distortions created by a trader's choice of accounting date, and abolishing double taxation caused by overlap periods.

8. The method of taxation of transition profits was designed following consultation, in order to reduce the impact of the change of basis on affected traders by mitigating the effect on benefits and allowances. The legislation as originally drafted may unintentionally prevent some traders from claiming certain tax reliefs in full due to the order of the steps of income tax calculation. The amendments remove this effect and allows all traders to claim these reliefs to the same extent as would otherwise have been the case.