

Office of Tax Simplification

Partnerships –Terms of Reference

Introduction

There are around 448,000 partnerships in the UK¹. Partnership taxation is not a designed, separate code but is based on general tax rules with some modifications. In most cases, the system does not treat the partnership as an entity; tax follows general law in treating partnerships as transparent, with tax being a responsibility of individual partners. This causes some administrative difficulties, for example, actual income and taxable income often differ due to the way profit sharing applies or administrative responsibilities can vary between partners as individuals and representative members.

Legislation relating to partnership taxation is not located in one place, but spread around the Taxes Acts, making it difficult to get an overview of partnership taxation. The capital gains charge for partnerships is based on an old Inland Revenue statement of practice from 1975 rather than specific legislation.

In most cases the same rules apply to a small firm of two partners as they do for major businesses with many hundreds of partners – a ‘one size fits all’ approach.

Some issues

It is questionable whether a tax code that has evolved in a piecemeal way and which has had to adapt to considerable business evolution is working efficiently for today’s partnerships. Are efficiency gains possible from a modernised tax system?

Partnerships have been widely used for tax avoidance, particularly to generate artificial losses, resulting in complex anti-avoidance rules that restrict sideways loss relief. Limited Liability Partnerships were introduced in 2000 and create issues for HMRC in terms of compliance and avoidance. LLPs are bodies corporate but are generally taxed as partnerships with their members taxed as partners.

Partnerships taxation involves extra administration for HMRC and advisers with two sets of forms needing to be returned and reconciled – one partnership return and an individual self-assessment form from each partner.

¹ 2012 The *Business Population Estimates (BPE) for the UK and Regions 2012* BIS
<http://www.bis.gov.uk/assets/biscore/statistics/docs/b/12-92-bpe-2012-stats-release.pdf>

The OTS Project

The Government has therefore commissioned the Office of Tax Simplification to carry out an initial review by autumn 2013 to identify the main complexities around partnership taxation, and recommend priority areas for a more detailed review leading to specific recommendations. The OTS's main focus will be on simplification but this does not mean that we will automatically be bringing forward proposals for change. Change can increase complexity and we will need to balance the benefits of a stable regime with the simplification dividends of any such changes. While the review will not look specifically into the non-tax legislation and policy surrounding the legal structures of partnerships, we may report on any issues raised during the review.

The review will:

- Identify all specific tax legislation relating to partnerships
- Review the administration of partnership taxation including filing of returns, payment of tax and penalties and information powers
- Review the HMRC guidance relating to partnerships
- Look across all the different taxes and review the evidence to identify which areas partnerships find most difficult, costly and burdensome
- Look at the complexities surrounding LLPs

An OTS review into partnership taxation could bring simplifications to partnerships and LLPs. The review should have regard to:

- The impact on partnerships, large and small, and partners across the UK
- International comparisons
- Interaction with non-tax legislation
- Fairness and consistency of treatment of taxpayers
- Any relevant anti avoidance measures being undertaken by HMRC
- The cost to the Exchequer: the OTS's remit is to bring forward recommendations that are broadly revenue neutral
- The Spending Review resource constraints on HMRC

The Office's work will be informed by consultation with interested parties, including forming and working with a consultative committee.