

OTS REVIEW OF THE TAXATION OF SMALL COMPANIES

Introduction

The Office of Tax Simplification (OTS) has agreed with the Chancellor and Financial Secretary to carry out a project reviewing the taxation of small companies. The overall aim of the project will be to develop recommendations for the Chancellor and Financial Secretary on how to simplify the system, increase certainty and reduce administrative burdens caused by the tax system.

In conducting this review, the office will provide an initial report to the Chancellor by Budget 2016 that:

- examines evidence and identifies the areas of the tax system that cause the most day-to-day complexity and uncertainty for small incorporated businesses
- recommends priority areas for simplification
- considers the impact of any simplification in these areas on other business sectors, particularly small unincorporated businesses

It may publish interim reports or calls for evidence during the review.

Terms of Reference

The review will include, but will not be limited to, consideration of:

- The differing requirements imposed by the tax system on small companies compared with unincorporated businesses (sole traders and partnerships)
- Whether and how tax affects the choice of business form and whether the choices faced by new and existing businesses can be simplified
- Whether there are simpler ways that small incorporated businesses could be taxed, including the potential for a look through basis for taxing small incorporated businesses.
- Simplification of tax policy for companies and how this compares with that for unincorporated businesses, including the relevance of a cash-accounting
- Simplification of administration in the context of HMRC's digital reforms, in particular:
 - Setting up a company when a business starts
 - Carrying out the day to day activities of the business, including record keeping requirements, returns, payments and the tax related choices that must be made by the business.
 - Closing the company when the business ceases
- The distortions between the personal and business tax systems

The Government has issued a discussion document on improving the effectiveness of the existing intermediaries' legislation (IR35) which will run in parallel to this review. Accordingly, the OTS review will not specifically consider IR35 but will liaise closely with that work stream.

Further guidance for the review

The familiar term “SME” (small and medium-sized enterprises) is sub-divided into medium (50 to 249 employees), small (10 to 49) and micro (1 to 9). The OTS review will concentrate on micro businesses, but will have regard to small businesses as well¹.

An indication of the significance of taxation to this population is given in the “Small Business Survey 2014” published by BIS in March 2015. This showed that 49% of the micro business population regard taxation as **an** obstacle to business success and that for the SME population as a whole 11% regard taxation as the **main** obstacle to business success.

In carrying out its review and developing its recommendations, the OTS should:

- Research widely among all stakeholders
- Involve the members of HMRC’s Administrative Burdens Advisory Board
- Aim to build consensus amongst small businesses, tax professionals and academics
- Take into account current and emerging trends amongst small businesses, including the implications of features such as working from the proprietor’s home, the growth of exporting amongst small businesses, and an increasing tendency to outsource work to other businesses.
- Consider all taxes and duties that impact on small businesses, including the administrative burdens imposed
- Consider its own previous recommendations on HMRC administration² regarding small businesses and how these have been progressed
- Consider the merit of framing reforms on a ‘default’ basis, such that a simpler basis is the assumed course for taxation but with scope for businesses to opt into a different basis
- Test the impact of the disincorporation relief³ introduced following a previous OTS report⁴
- Be consistent with the principles for a good tax system, including fairness and efficiency
- Take account of international experience
- Be consistent with the principles and design of HMRCs Making Tax Easier reforms, including digital tax accounts, integrated reporting and payment
- Take account of the interface with other Government obligations on small businesses, including BIS regulation such as company registration, reporting and statutory accounting
- Consider revenue implications of individual recommendations

¹ In its previous reports, the OTS coined the term ‘nano’ business to describe those with turnover under £30,000 (some 2 million in the UK). These are unlikely to be VAT registered and would have none, one or two employees (typically part time).

² OTS February 2012, Small Business Tax Review: Final report, HMRC administration

³ Finance Act 2013, section 58

⁴ OTS February 2012, Small Business Tax Review: Final report, Disincorporation relief