

# Association of Accounting Technicians response to the Office of Tax Simplification Discussion Paper: “Lookthrough taxation”

# Association of Accounting Technicians response to the Office of Tax Simplification Discussion Paper: “Lookthrough taxation”

---

## 1. Introduction

- 1.1. The Association of Accounting Technicians (AAT) is pleased to have the opportunity to respond to the Office of Tax Simplification’s (OTS) discussion paper “Lookthrough taxation – A discussion paper” published 18 July 2016 (the paper).
- 1.2. AAT is submitting this response on behalf of our membership and from the wider public benefit of achieving sound and effective administration of taxes.
- 1.3. AAT has focussed on the operational perspective, entering into comment in order to add value or highlight aspects that need to be considered further.
- 1.4. In order to inform the response preparation process a handpicked group of 10 of AAT’s senior licensed accountants and thought leaders met with the Tax Director of the OTS in August to discuss and consider the contents of the paper in a round-table environment.
- 1.5. The outcomes arising from the round-table event (the event) have been extensively used to inform the production of this response.
- 1.6. AAT thanks all of those involved in the event, especially the Tax Director of the OTS and looks forward to the Office’s publication of its October Conclusion Document.

## 2. Executive summary

- 2.1. AAT acknowledges and endorses the OTS’s objective to provide genuine simplification in the tax system. However, we remain unconvinced that Lookthrough will act as a genuine vehicle to achieve this.
- 2.2. The introduction of a Lookthrough regime would merely add another layer of complexity to the taxation system. The current method of calculating a close company’s corporation tax, the completion of the associated corporation tax return and supporting schedules were already considered to be a simple process (3.5, below)
- 2.3. There is a real danger under Lookthrough that entrepreneurship and company growth could be stifled if retained profits of small companies are subject to the same rate of tax and National Insurance as distributed profits.
- 2.4. If a form of Lookthrough is to be introduced, retained profits should not be taxed at a rate above the prevailing rate of Corporation Tax (3.10, below).
- 2.5. There is no merit in adding back to trading profits the salaries paid to the shareholding officer(s) of a small company (3.14, below).

- 2.6. Those present at the event were unanimously opposed to the mandation of Lookthrough (3.19, below).
- 2.7. However, if Lookthrough is not mandated it is unlikely that there would be any enthusiasm to adopt Lookthrough amongst owner-managers of small companies, once the administration, cashflow and tax implications were understood (3.21, below)
- 2.8. The cash basis of accounting will not introduce a positive step in the direction of tax simplification. The requirement for incorporated businesses to file accounts compiled in accordance with accounting standards negates any benefit that might otherwise be derived (3.23, below).
- 2.9. AAT cannot see that Lookthrough can deliver a worthwhile level of tax-simplification to UK-Plc. As one attendee at the event said: *"We don't even itemise corporation tax calculations on clients' bills as this would take more time than the calculations themselves."* (3.24 & 3.25, below)

### 3. **AAT response to the consultation paper**

- 3.1. The following paragraphs outline AAT's response to the proposals set out in the consultation paper.

**Question 1: Do you agree with the five key issues above? If not how would you change or add to them?**

- 3.2. AAT is satisfied that at a strategic level the five bullet points listed under "Key Issues" (page 2, the paper) covering "who, how, tax consequences, optional or compulsory and simplification" are the correct points to have in mind when considering the viability of Lookthrough.

**Question 2: Do you agree with the OTS's conclusion from the small company taxation review of the characteristics of companies that could materially benefit from the simplification offered by lookthrough? and**

**Question 3: Do you think lookthrough would have an impact on growth companies if applied to them? If so, how?**

- 3.3. AAT acknowledges that the characteristics of the cohort of companies set out as four bullet points under "Who would Lookthrough apply to?" (page 2, the paper) would be the correct hallmarks to identify companies most likely to "benefit".
- 3.4. In responding to question 2, it should be noted, AAT does not accept that Lookthrough is a genuine means to achieving tax simplification for owner-managers of small companies.
- 3.5. Those present at the event considered, almost without exception, that the existing taxation of small companies' regime is not overly complex. The prevailing view was that dealing with the tax affairs of a close company is merely a minor and incidental by-product of the statutory accounts production process.

- 3.6. In fact, it was considered that the introduction of Lookthrough -another approach to the taxation of a small company - was likely to add another layer of complexity.
- 3.7. AAT is pleased to note that OTS acknowledges that the Lookthrough model threatens to reduce the monies available (retained profits) for growth-companies (pages 2 & 3, the paper) and is encouraged by the OTS's undertaking that "we will work with the relevant Government departments and stakeholders to ascertain the impact of Lookthrough..."
- 3.8. There is no doubt that if the retained profits of a growth-company are taxed at the same rate as they would be in the instance of a sole-trader this would lead to a reduction in the funds on hand.
- 3.9. Consequently, either directly, if a company is unable to source additional capital from elsewhere, or indirectly if a company has to borrow on the open market (and pay the associated costs) growth-companies will be less competitive.
- 3.10. One way to address the issue of overtaxing profits retained within the company's wrapper is to subject such profits to a lower rate of tax, say 20% and only levy a higher, balancing tax charge, at the time of a future distribution to the shareholder(s).

**Question 4: Leaving aside your views on whether lookthrough is a good or a bad idea, should the target group of companies be defined according to a turnover limit like the cash accounting limit? Or are there other methods that would better target a group of potential lookthrough companies? Do you think lookthrough should have a limit at all?**

- 3.11. Leaving aside the fact that those present showed little, if any, enthusiasm for Lookthrough, the widely held view is that the target group of companies should be defined by turnover, limited in the same order as that under cash accounting.
- 3.12. There was no support expressed for an upper limit.
- 3.13. While there might be other limits and ceiling which could be chosen, their setting would only lead to a greater level of tax complexity. That said, OTS should give consideration as to whether or not there might be scope to adopt the FRS 105 (The Financial Reporting Standard applicable to the Micro-entities Regime) turnover ceiling of £632,000.

**Question 5: If allocation is made, should salaries be added back or left to stand? and**

**Question 6: Are there other significant 'other issues' that need to be considered beyond the five noted above?**

- 3.14. As salaries have already been reported and subjected to tax in real time it is considered simplest, from a tax perspective, if they were not then added back for Lookthrough purposes.
- 3.15. AAT does not have knowledge of any other significant issues and does not have comments to make in respect of how one would test to exclude investment companies.

**Question 7: What other types of income do we need to consider for lookthrough? and**

**Question 8: Do you agree with the outline treatments above or do you have any suggestions on how they should be treated differently?**

- 3.16. AAT does not have any other types of income to suggest for consideration under Lookthrough.
- 3.17. AAT is pleased to note in the opening sentence under “what tax consequences would ensue...” (page 4, the paper) that OTS accepts that calculating the amount of tax due is relatively simple. While it has to be accepted that matters such as directors’ loan accounts, expenses and P11Ds add layers of complexity, it was also the widely held view of those present at the event that the calculation of *corporation tax was a minor consequence of preparing the statutory accounts, see also 3.26 (below)*
- 3.18. In response to question 8; leaving aside that those present showed little, if any enthusiasm for Lookthrough, AAT agrees with the outline treatments and does not have any suggestions on how they should be treated differently.

**Question 9: Do you think lookthrough, if it is introduced, should be optional/default or compulsory? Do you have any further points for your preferred route beyond those mentioned above?**

- 3.19. The unanimous view of all AAT participants is, if Lookthrough is to be taken forward it should only be on an optional basis.
- 3.20. Issues, such as the negative impact that a reduction of cashflow would have on growth-companies and the disadvantaging of entrepreneurs who are often higher rate taxpayers, were considered to be too significant to ignore for the well-being of the UK economy as a whole.
- 3.21. Without mandation it is highly likely that once owner-managers of small companies understood the tax, administration burdens and cashflow issues the take up of Lookthrough would be extremely low.

**Question 10: Would cash accounting be a useful simplification for lookthrough companies? and**

**Question 11: Would cash accounting be useful to companies even if they still had to produce a corporation tax return?**

- 3.22. Ignoring reporting requirements imposed on small companies introducing cash accounting as a starting point for the calculation of taxable profits could be a useful simplification.
- 3.23. However, when preparing statutory accounts it is not possible to ignore accounting standards, such as FRS102 and 105 and the reporting disciplines that they impose. This being the case, the reporting of taxable profits using cash accounting as a basis of calculation cannot be seen to be a useful aid to simplification.

3.24. Taking as previously acknowledged (3.17, above) that the calculation of tax and the preparation of the related tax returns for a small company is actually a relatively simple process and a small part of the accounting period end statutory accounts production process, it is hard to see what benefits would accrue from an introduction of a cash accounting.

**Question 12: What do YOU think? Can lookthrough deliver simplification?**

3.25. As repeatedly stated throughout this paper, the calculation of corporation tax is minor and incidental to the production of the statutory accounts at the end of an accounting period.

3.26. As one attendee at the event put it: *"We don't even itemise corporation tax calculations on clients' bills as this would take more time than the calculations themselves."*

3.27. For all of the reasons given above AAT cannot see that Lookthrough can deliver a worthwhile level of tax-simplification to UK-Plc.

**4. About AAT**

4.1. AAT is a professional accountancy body with approximately 50,000 full and fellow members and 80,000 student and affiliate members worldwide. Of the full and fellow members, there are over 4,200 licensed accountants who provide accountancy and taxation services to individuals, not-for-profit organisations and the full range of business types.

4.2. AAT is a registered charity whose objectives are to advance public education and promote the study of the practice, theory and techniques of accountancy and the prevention of crime and promotion of the sound administration of the law.

**5. Further information**

If you have any questions or would like to discuss any of the points in more detail then please contact Aleem Islan, AAT Technical Consultation Manager, at:

E-mail: [consultation@aat.org.uk](mailto:consultation@aat.org.uk) Telephone: 020 7397 3088

Association of Accounting Technicians  
140 Aldersgate Street  
London  
EC1A 4HY