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Sent by email

Dear Jonathan and Jo

MAKING TAX DIGITAL SMALL BUSINESS REVIEW

Following the announcement of 19 December 2022, ICAEW has had very positive engagement with your teams on the review of how making tax digital for income tax self assessment (MTD ITSA) could be shaped to suit the needs of smaller businesses (self-employed and landlords).

Anita Monteith, Caroline Miskin and I had a meeting with the MTD team and we facilitated a virtual roundtable with the MTD team and 11 ICAEW members in practice. The purpose of this letter is to summarise the key points raised at these meetings.

ICAEW remains wholly supportive of the digitalisation of businesses and practices; indeed many of our members are now focusing on the business case for widespread adoption of digitalisation rather than MTD.

However, we consider that this also gives an opportunity for fresh thinking on MTD ITSA policy. When first announced in 2015, this project was called making tax simpler and we need to return to that core principle and message. Eight years later, MTD ITSA has become mired in controversy and the credibility of the project and the ‘MTD brand’ has been severely, if not irretrievably, undermined. To maximise support by business, the project needs a rethink and a rebrand, focused on the original aims, namely to deliver productivity benefits from the adoption of software and digital record keeping and making it simpler for taxpayers to comply with their tax obligations.

This fresh thinking needs to be applied to all taxpayers, not just those with turnover below £30,000. The population of taxpayers below this threshold does indeed have certain characteristics such as higher percentages of landlords, taxpayers with another source of income and those earning below the personal allowance. They are more likely to find the cost of software and/or agent fees disproportionate. However, many of them will encounter exactly the same problems with MTD ITSA as taxpayers with a higher turnover. The introduction of another cliff edge in the tax system is potentially unhelpful.

We suggest that the project is refocussed on what can realistically be delivered in 2026 and on digital record keeping and filing from software.

The implementation plan that we have seen suggests that there is a significant risk that the necessary functionality may not be delivered by 2026; some is not scheduled to be delivered until 2025/26 or 2026/27. It is difficult to see how many of the very difficult issues, such as the need for multiple agents and the reporting of income from jointly held property, will be resolved in sufficient time to allow for an adequate pilot. We are also extremely concerned about HMRC's capacity to deliver the necessary support to taxpayers and agents given the continued pressure on HMRC's budget and headcount, Any changes HMRC makes to its systems should have as an essential outcome a reduction in the need for taxpayers and agents to contact HMRC for help and support As currently designed MTD ITSA will significantly increase the number of touchpoints and amount of contact from taxpayers who have difficulty filing or receive submission penalties.

In particular, we consider that the administrative burden associated with quarterly updates is disproportionate and needs a rethink. Even when a taxpayer is maintaining digital records on a regular basis, having to ensure that these records are complete and checked by specific quarterly deadlines adds extra compliance burdens, especially where a bookkeeper or agent is involved as we expect in the majority of cases. Quarterly updates provide HMRC with little or no assurance about the quality of the underlying digital records. One of the reasons why quarterly reports are getting all the attention is because they can lead to late submission penalties. Record keeping penalties are not being reformed despite that being the primary behaviour that needs to change.

We suggest that HMRC starts by introducing the requirements to maintain digital records and to submit details of income from self-employment and property directly from software but that the current annual reporting cycle is maintained. Quarterly reporting could be considered in the future, once an annual system is established, if that does not lead a sufficient improvement in record keeping. We anticipate, however, that given the increased impetus towards digitalisation, that requiring the use of software and digital records should provide most of the benefits sought. More frequent MTD ITSA reporting could be considered for those VAT registered businesses that already report on a quarterly cycle. Quarterly updates could be optional.

This approach would have the added benefit of changing the narrative on MTD ITSA and show that HMRC and government are prepared to work together with stakeholders to achieve an outcome which both supports and works with the grain of business. It would allow HMRC to assess the impact of introducing digital record keeping requirements and the use of software separately from the impact of quarterly reporting. It would change the focus of the discussion from quarterly reports back on to digital records and filing from software. Finally, it would support delivery by 2026 as many of the implementation problems, for example multiple agents, would be eased considerably if the quarterly reporting requirement were dropped or postponed.

We would welcome the opportunity to speak with you further.

Yours sincerely

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