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Basis Period Reform - the transitional year (2023/24)

Richard Jones (ICAEW Tax Faculty) and Daniel Shaw (HMRC)

Presenters



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Today's Speaker
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HMRC



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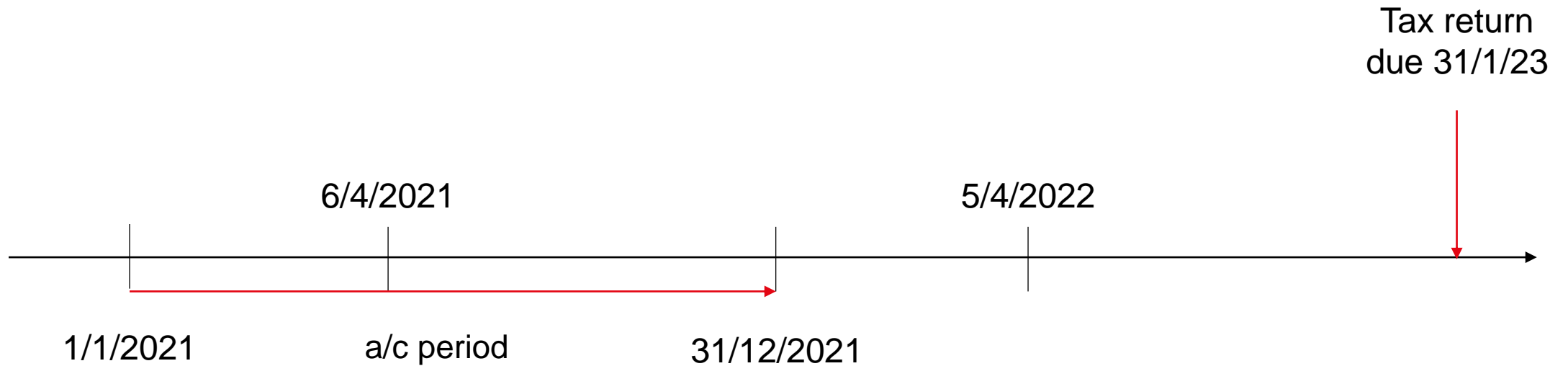
Recording

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Agenda

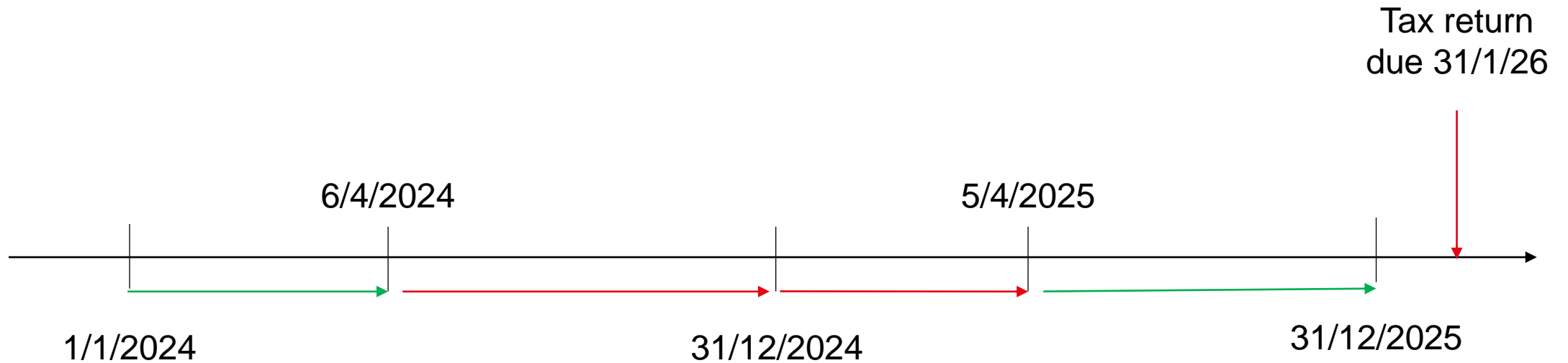
- Brief re-cap on basis period reform
- What happens in the transitional tax year (2023/24) and next four years?

The basis period method (31 December y/e)



Profits of the accounting period ended 31 December 2021 are taxed in the tax year 2021/22
Final tax payment made just over a year after end of accounting period

New basis of taxation (31 December y/e)

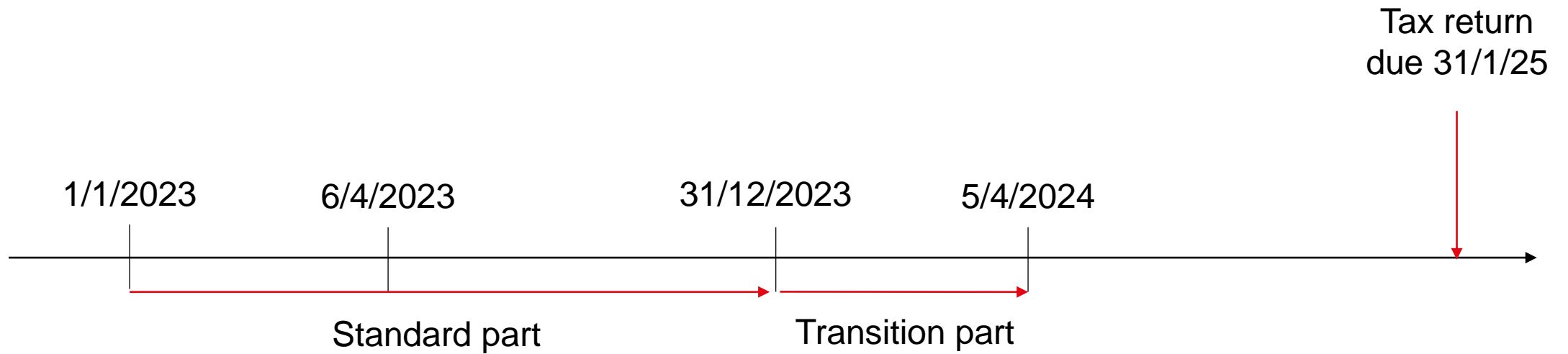


In 2024 – 25, profits taxed are:

- time-proportioned profits from 2024 AP (6 April 2024 to 31 December 2024); plus
- time-proportioned profits from 2025 AP (1 January 2025 to 5 April 2025)

Note: Any capital allowances claimed are included in the results to be apportioned from each AP

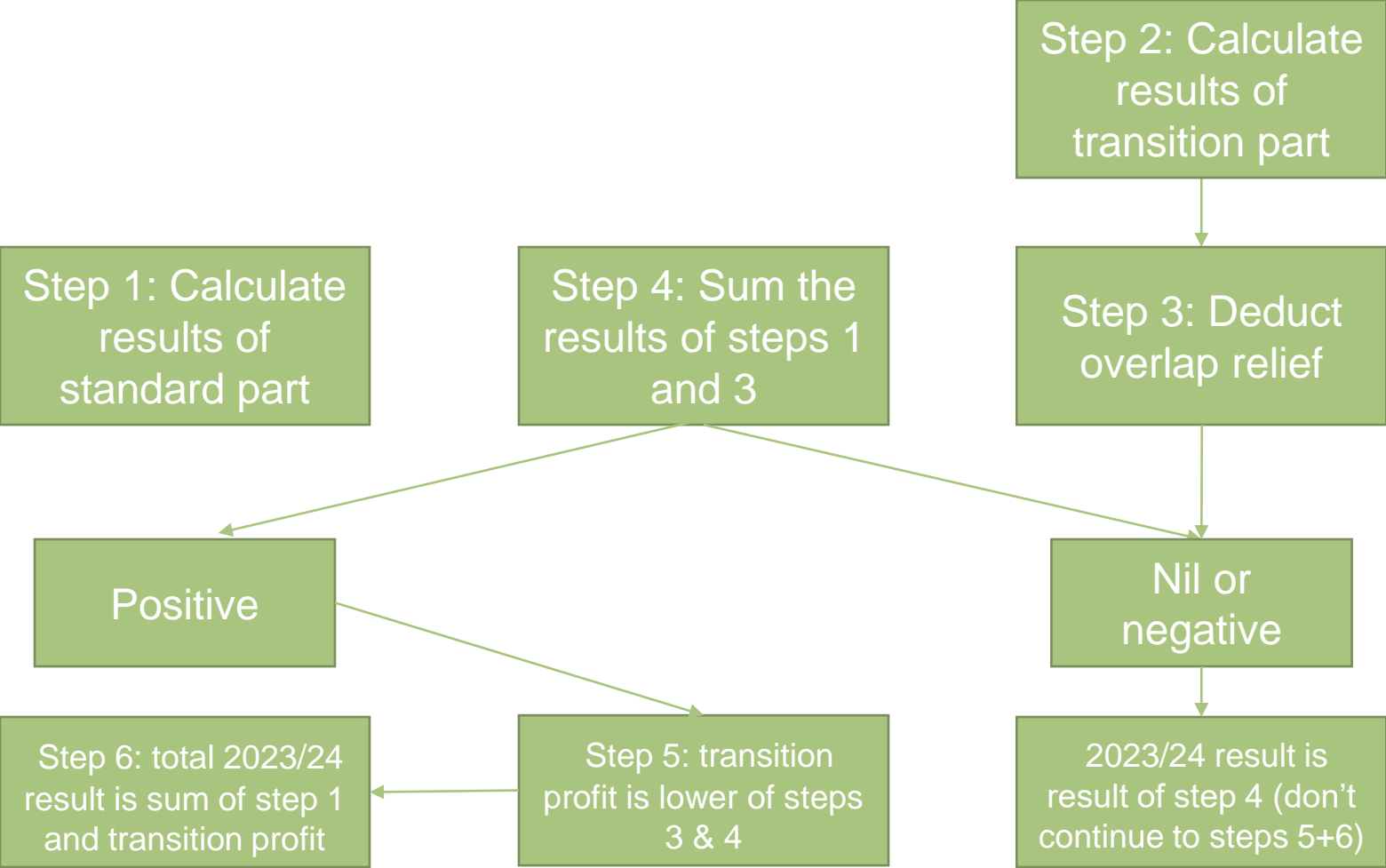
Transition year 2023 - 24 (31 December y/e)



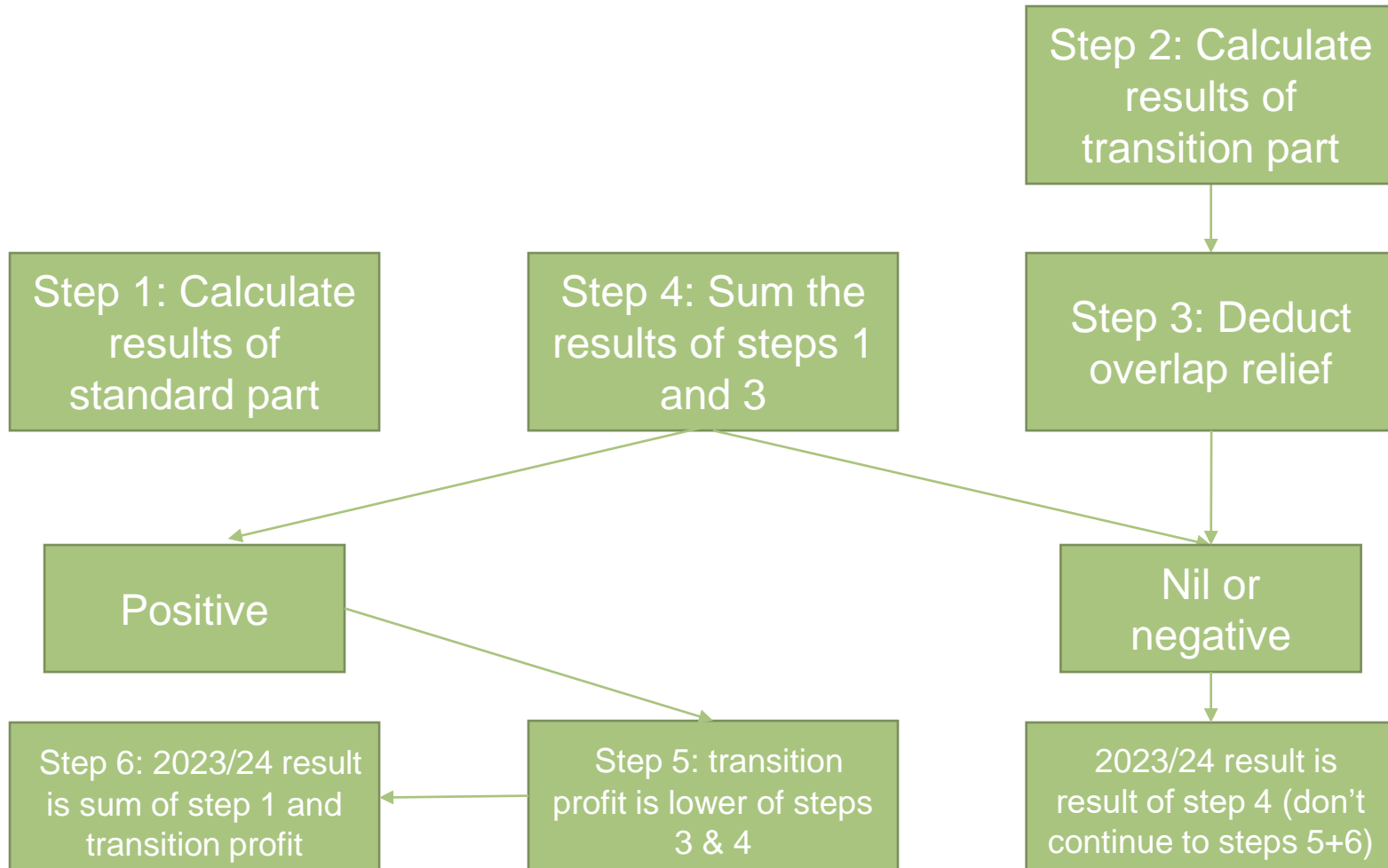
In 2023 – 24, taxable profits are calculated as follows:

1. Calculate standard part – the first 12 months' results from the end of the final AP taxed in 2022-23 (eg the 12 month period ending 31 December 2023)
2. Calculate transition part – Profits up to 5 April 2024 (in this case, 96 days' worth of the 2024 AP result)
3. Deduct overlap relief from 2. above

Calculating transitional year results



Calculating transitional year results



Example 1:

- Standard part profit = £100k
- Transition part profit = £30k
- Overlap relief = £20k

Step 1: £100k

Step 2: £30k

Step 3: £10k

Step 4: £110k

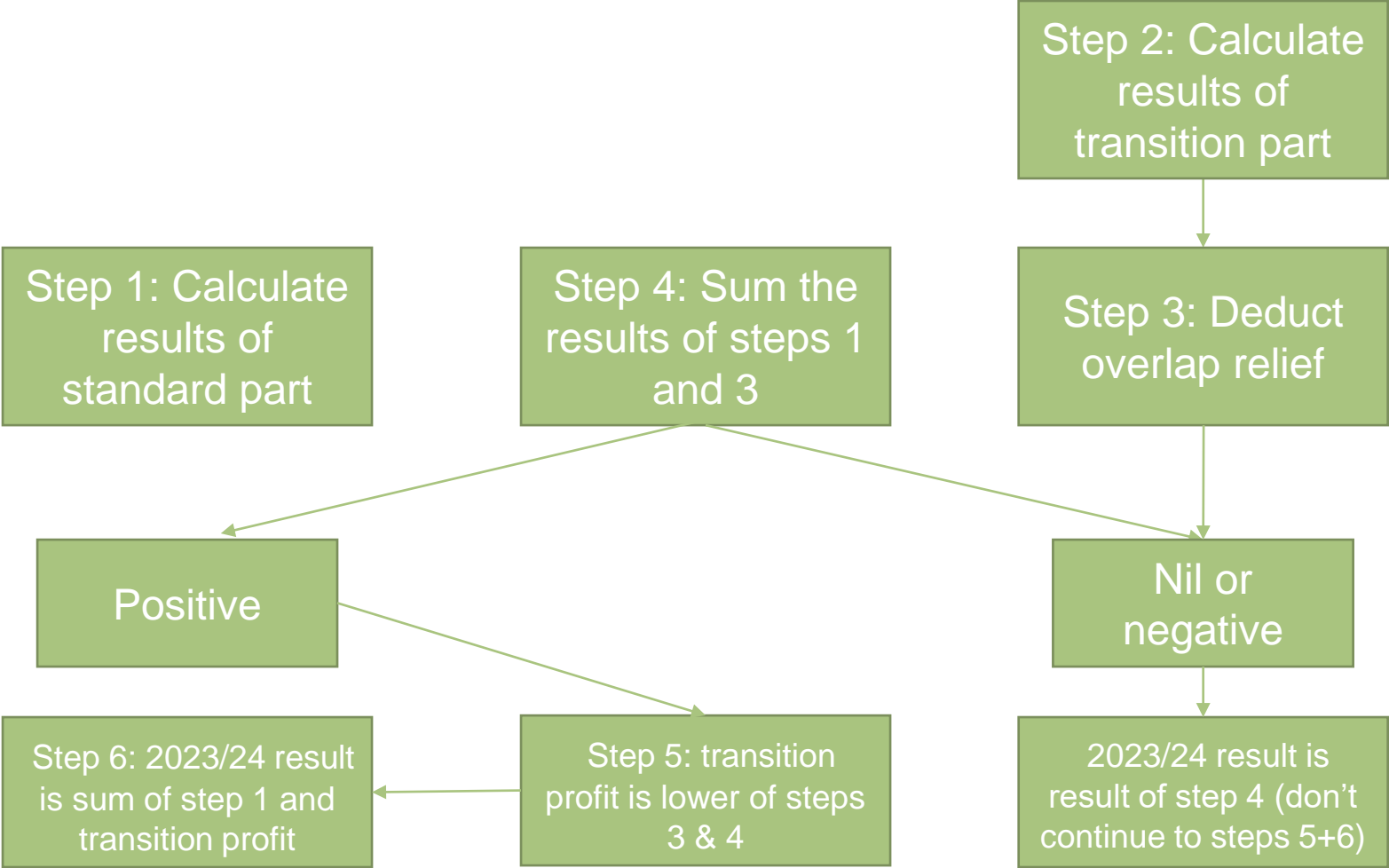
Step 5: £10k (transition profit)

Step 6: £100k + £10k = £110k

Standard profit £100k

Transition profit £10k

Calculating transitional year results



Example 2:

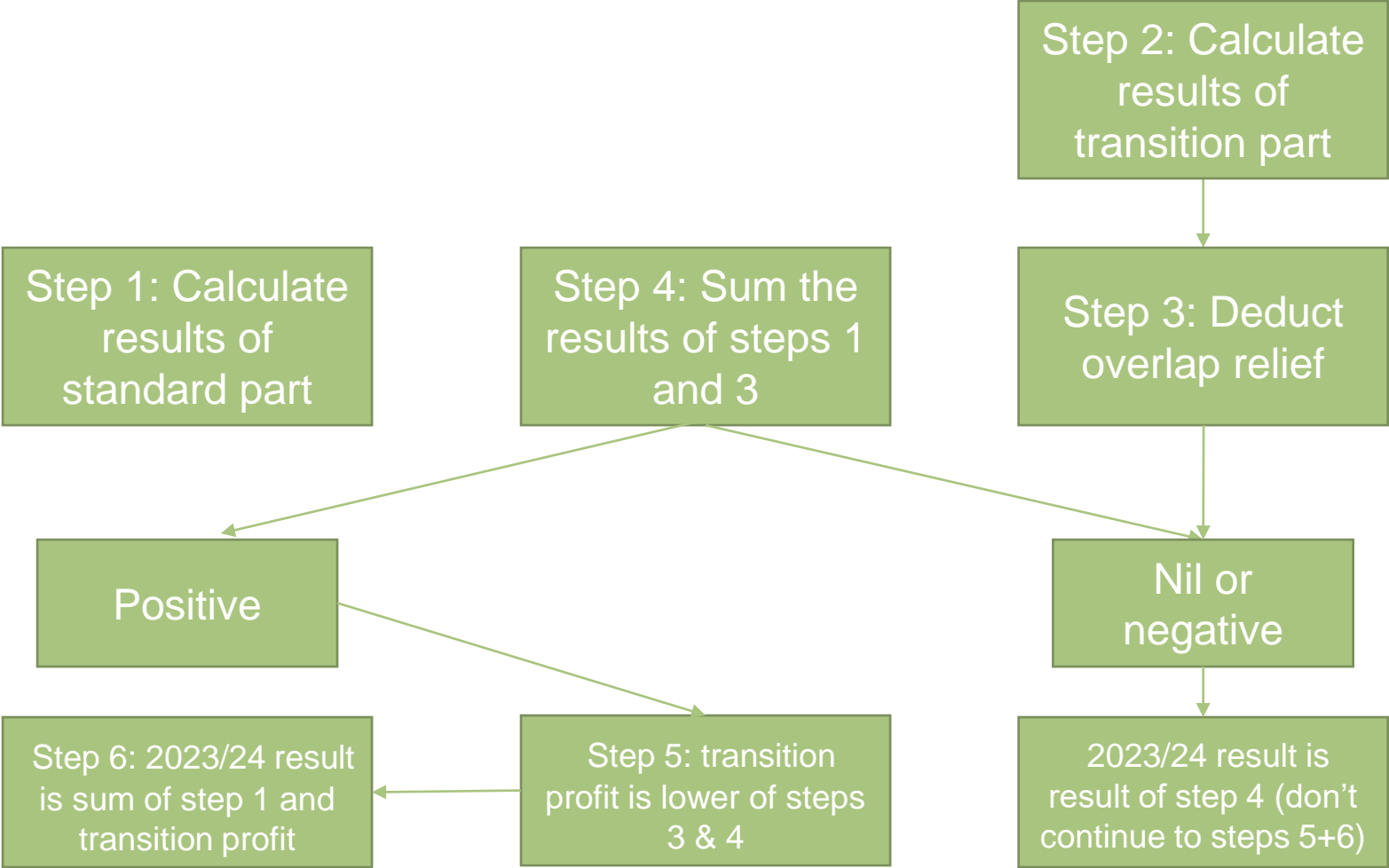
- Standard part profit = £100k
- Transition part loss = (£10k)
- Overlap relief = £20k

Step 1: £100k
Step 2: (£10k)
Step 3: (£30k)
Step 4: £70k

No steps 5 + 6

Taxable profit £70k
No transition profit

Calculating transitional year results



Example 3:

- Standard part loss = (£100k)
- Transition part profit = £10k
- Overlap relief = £20k

Step 1: (£100k)
Step 2: £10k
Step 3: (£10k)
Step 4: (£110k)

No steps 5 + 6

Allowable loss £110k
No transition profit

Use of losses in transitional year

The loss that can be treated as a terminal loss is:

- where overlap relief turns a profit for 2023-24 into a loss, the amount of the loss arising due to the deduction of overlap profits
- where the loss for 2023-24 has become greater, the amount by which the loss has increased due to the deduction of overlap profits

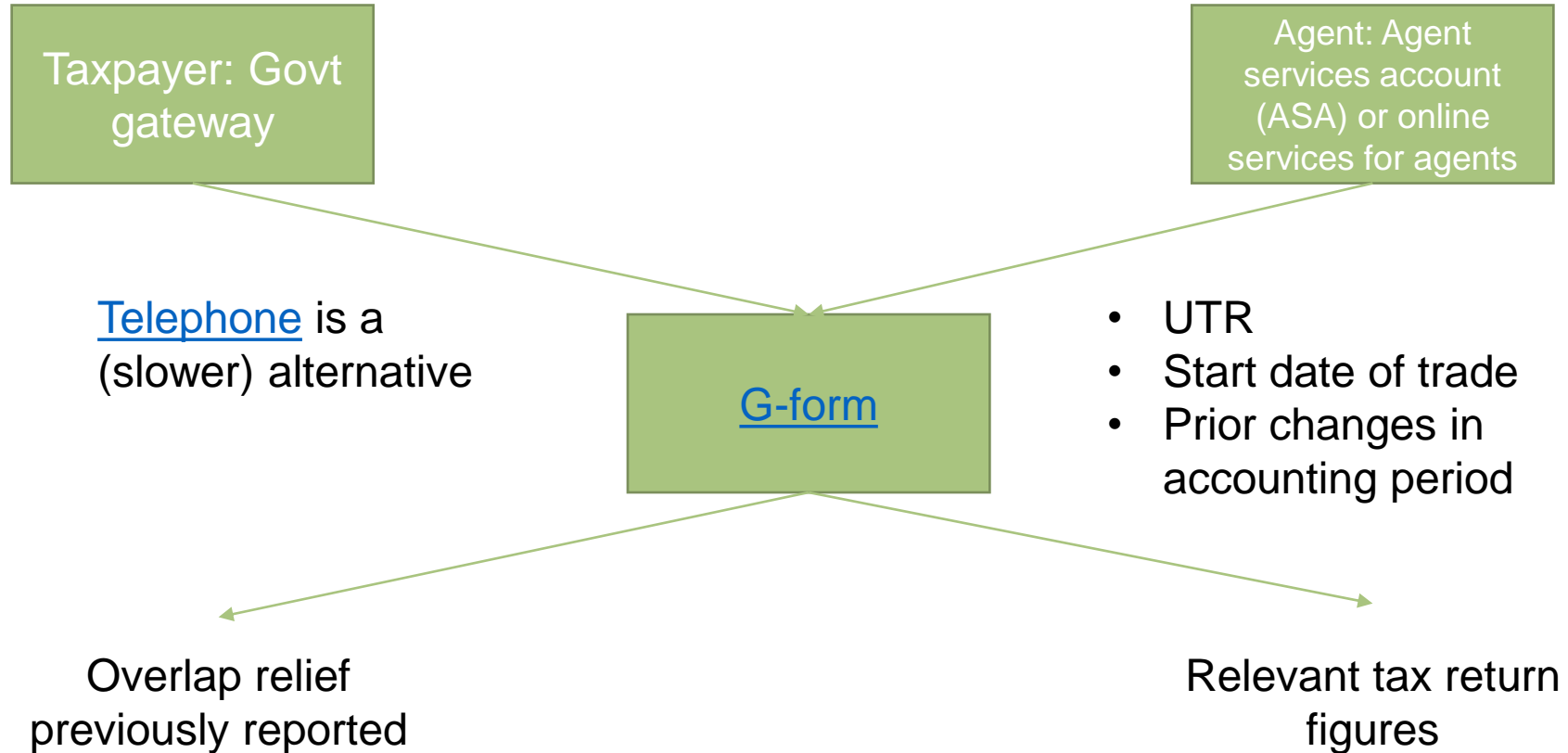
This allows the loss to be carried back up to three years, on a last in first out basis.

Use of losses – example 3

- Standard part loss = (£100k)
- Transition part profit = £10k
- Overlap relief = (£20k)

Of the £110k loss, only £20k can be treated as terminal loss

Requesting overlap relief info from HMRC



Spreading of transition profits

Example 1 – Transition profit of £10,000

	2023/24	2024/25	2025/26	2026/27	2027/28
Standard	£2,000	£2,000	£2,000	£2,000	£2,000
Trade ceases in 2025/26	£2,000	£2,000	£6,000		
Elect to allocate more to 2024/25	£2,000	£5,000	£1,000	£1,000	£1,000

Notes:

- No spreading if business changes its year end to 31 March / 5 April prior to 2023 – 24
- But spreading is available if year end change to 31 March / 5 April is in 2023 – 24
- Transition profits ignored for farmers' and creative artists' averaging calculations (see example later)

Change of year end in transitional year

- Changing a business' year end to 31 March / 5 April 2024 DOES NOT prevent the transitional profit from being spread
- Only impact is that the calculation of the transitional profit may change a little
- Also, it is possible in 2023/24 to have an accounting period longer than 18 months
- Though **LLPs** can still only extend APs once every 5 years and then up to a maximum of 18 months. APs can, however, be shortened at any time.
- For capital allowances, an AP cannot be more than 18 months long. Any AP longer than that must be split into two periods being:
 - the first 12 months; and
 - the remainder of the accounting period

18 month-plus accounting period example

23-month accounting period to 31 March 2024

12 months to 30 April 2023

11 months to 31 March 2024

Standard part profit = 12/23
of the results of the AP

Transitional part profit = 11/23
of the results of the AP

12-month CA period

11-month CA period

NB not pro-rated across the whole AP. This means that additions, disposals etc are separated between pre and post 30/4/23

Transitional period results: with no year end change

- David has a 30 September year end and the following profits:
 - Year ended 30 September 2023: £50,000
 - Year ended 30 September 2024: £60,000
 - Overlap relief: £20,000

- Taxable profits in 2023/24

Standard part		£50,000
Transitional part (£30k - £20k)	£10,000	
Spread over five years		<u>£2,000</u>
Taxable in 2023/24		£52,000

Transitional period results: with year end change

- David has the following profits:
 - 18 month period ended 5 April 2024: £90,000
 - Overlap relief: £20,000

- Taxable profits in 2023/24

Standard part (12/18 x £90,000)		£60,000
Transitional part (6/18 x £90,000)	£30,000	
Less: overlap relief	<u>(£20,000)</u>	
	£10,000	
Spread over five years		<u>£2,000</u>
Taxable in 2023/24		£62,000

What does the transitional year look like on the ITSA tax return?

- Key boxes on the SA103F for affected taxpayers:
- Box 64/65 profit/loss
- Box 66/67 basis period dates
- Box 68 profit/loss adjustment
- Box 73.1 transition profit/loss
- Box 73.2 overlap relief

(box 46 + box 59 + box 60) £ <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> . <input type="text"/> <input type="text"/>		64 Net business profit for tax purposes (if box 47 + box 61 minus (box 48 + box 63) is positive) £ <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> . <input type="text"/> <input type="text"/>
62 Income, receipts and other profits included in business income or expenses but not taxable as business profits £ <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> . <input type="text"/> <input type="text"/>	65 Net business loss for tax purposes (if box 48 + box 63 minus (box 47 + box 61) is positive) £ <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> . <input type="text"/> <input type="text"/>	

SA103F 2024

Page SEF 3

Calculating your taxable profit or loss (continued)

Basis period reform simplifies the tax rules for the self-employed and partners so that a business's profit or loss for a tax year is measured in the tax year itself, regardless of its accounting dates or whether a business has recently started trading. This removes the complex basis period rules and stops the profits being taxed twice, as may have occurred under the old rules (overlap relief).

You may be affected by basis period reform if you had an accounting date that was not on or between 31 March and 5 April in the 2022–23 tax year. If you do not have a transition profit or loss to report, you only need to consider completing boxes 66 to 73, 74, 75 and 76. Please read the 'Self-employment (full) notes' and fill in the boxes below that apply.

66 Date your basis period began DD MM YYYY <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/>	Only complete boxes 73.1 to 73.4 if you have a basis period transition profit or loss – read the notes
67 Date your basis period ended DD MM YYYY <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/>	
68 If your basis period is not the same as your accounting period, enter the adjustment needed to arrive at the profit or loss for the basis period – if the adjustment needs to be taken off the profit figure, put a minus sign (-) in the box – do not include any transition profit or loss in this box, see box 73.1 £ <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> . <input type="text"/> <input type="text"/>	73.1 Profit or loss of the transition part of the basis period £ <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> . <input type="text"/> <input type="text"/>
	73.2 Overlap relief used on the transition part of the basis period this year £ <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> . <input type="text"/> <input type="text"/>
	73.3 Spread of the transition profit treated as arising in this tax year – read the notes £ <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> <input type="text"/> . <input type="text"/> <input type="text"/>

What does the transitional year look like on the ITSA tax return?

- Box 64/65 – profit or loss of the accounting period
 - Latest submitted accounts on “main” set of pages
 - Earlier accounts on “supplementary” set(s)
 - Do not have to submit pages for APs ending after 5/4/24
- Box 66/67 – whole basis period
 - Ends 5/4/2024 for continuing businesses
 - Ceasing? – ends on cessation date (no transition part)
- Box 68 – adjustment of box 64/65 figure to standard profit/loss
- Box 73.1 – transition profit/loss
- Box 73.2 – overlap relief (box 69 for cessations / unaffected taxpayers)

What does the transitional year look like on the ITSA tax return?

- 3 likely scenarios:
 1. No change of accounting date, stay non-aligned
 2. Change of accounting date, with one long accounting period to 31/3 or 5/4
 3. Change of accounting date, with two accounting periods:
 - 12 months to old accounting date
 - Short period to 31 March or 5 April

Scenario 1 – No change of accounting date

Example: 31 December year end –

- Complete SA103F as normal for 31/12/2023 up to box 64/65
- Box 64/65 is AP and standard profits/loss
- Box 66/67 are 1/1/2023 and 5/4/2024
- Likely no box 68 entry – watch early years of trading
- Transition profit enter in box 73.1 – no need to submit SA103F for 31/12/2024
- Overlap relief enter in box 73.2

Scenario 2 – Change of accounting date, one long accounting period

Example: 31 December year end extended to 31 March –

- Complete SA103F for long AP to 31/3/2024 up to box 64/65
- Box 64/65 is AP profits/loss
- Box 68 adjusts AP p/l to standard profit/loss – here minus 3/15 months (91/456 days)
- Box 66/67 are still 1/1/2023 and 5/4/2024 (unless early years)
- Transition profit enter in box 73.1 – likely reversal of box 68 figure
- Overlap relief enter in box 73.2

Scenario 2 – Change of accounting date, one long AP

Profits 15 months to 31/3/2024 £40,000

Standard profit

$$40,000 \times 365/456 = £32,017$$

Box 64 = 40,000, so box 68 = £-7,983

Transition profit in box 73.1:

$$40,000 \times 91/456 = £7,983$$

64	Net business profit for tax purposes (if box 47 + box 61 minus (box 48 + box 63) is positive)	£ <input type="text" value="4"/> <input type="text" value="0"/> <input type="text" value="0"/> <input type="text" value="0"/> <input type="text" value="0"/> <input type="text" value="0"/> <input type="text" value="0"/> <input type="text" value="0"/> · <input type="text" value="0"/> <input type="text" value="0"/>
65	Net business loss for tax purposes (if box 48 + box 63 minus (box 47 + box 61) is positive)	£ <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> · <input type="text" value="0"/> <input type="text" value="0"/>
66	Date your basis period began DD MM YYYY	<input type="text" value="0"/> <input type="text" value="1"/> <input type="text" value="0"/> <input type="text" value="1"/> <input type="text" value="2"/> <input type="text" value="0"/> <input type="text" value="2"/> <input type="text" value="3"/>
67	Date your basis period ended DD MM YYYY	<input type="text" value="0"/> <input type="text" value="5"/> <input type="text" value="0"/> <input type="text" value="4"/> <input type="text" value="2"/> <input type="text" value="0"/> <input type="text" value="2"/> <input type="text" value="4"/>
68	If your basis period is not the same as your accounting period, enter the adjustment needed to arrive at the profit or loss for the basis period – if the adjustment needs to be taken off the profit figure, put a minus sign (-) in the box – do not include any transition profit or loss in this box, see box 73.1	£ <input checked="" type="checkbox"/> <input type="text" value="-"/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value="7"/> <input type="text" value="9"/> <input type="text" value="8"/> <input type="text" value="3"/> <input type="text" value="0"/> <input type="text" value="0"/>
73.1	Profit or loss of the transition part of the basis period	£ <input checked="" type="checkbox"/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value="7"/> <input type="text" value="9"/> <input type="text" value="8"/> <input type="text" value="3"/> <input type="text" value="0"/> <input type="text" value="0"/>
73.2	Overlap relief used on the transition part of the basis period this year	£ <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> <input type="text" value=""/> · <input type="text" value="0"/> <input type="text" value="0"/>

Scenario 3 – Change of accounting date, two accounting periods

Example: 31 December year end shortened to 31 March –

- Complete “supplementary” SA103F for first AP 12m to 31/12/2023, up to box 64/65
- Complete “main” SA103F for second AP 3m to 31/3/2024
- Box 64/65 is second AP profits/loss – may equal transition profit/loss
- Box 68 adjusts second AP p/l to standard profit/loss
- Box 66/67 are still 1/1/2023 and 5/4/2024 (unless early years)
- Transition profit enter in box 73.1 – likely equal to box 64/65 figure
- Overlap relief enter in box 73.2

Scenario 3 – Change of accounting date, two APs

Profits –

- year to 31/12/2023 £32,000
- 3 months to 31/3/2024 £8,000

Box 64 = £8,000 (2nd period on main return)

Standard profit is 32,000, so box 68 = £24,000

Transition profit in box 73.1 = £8,000

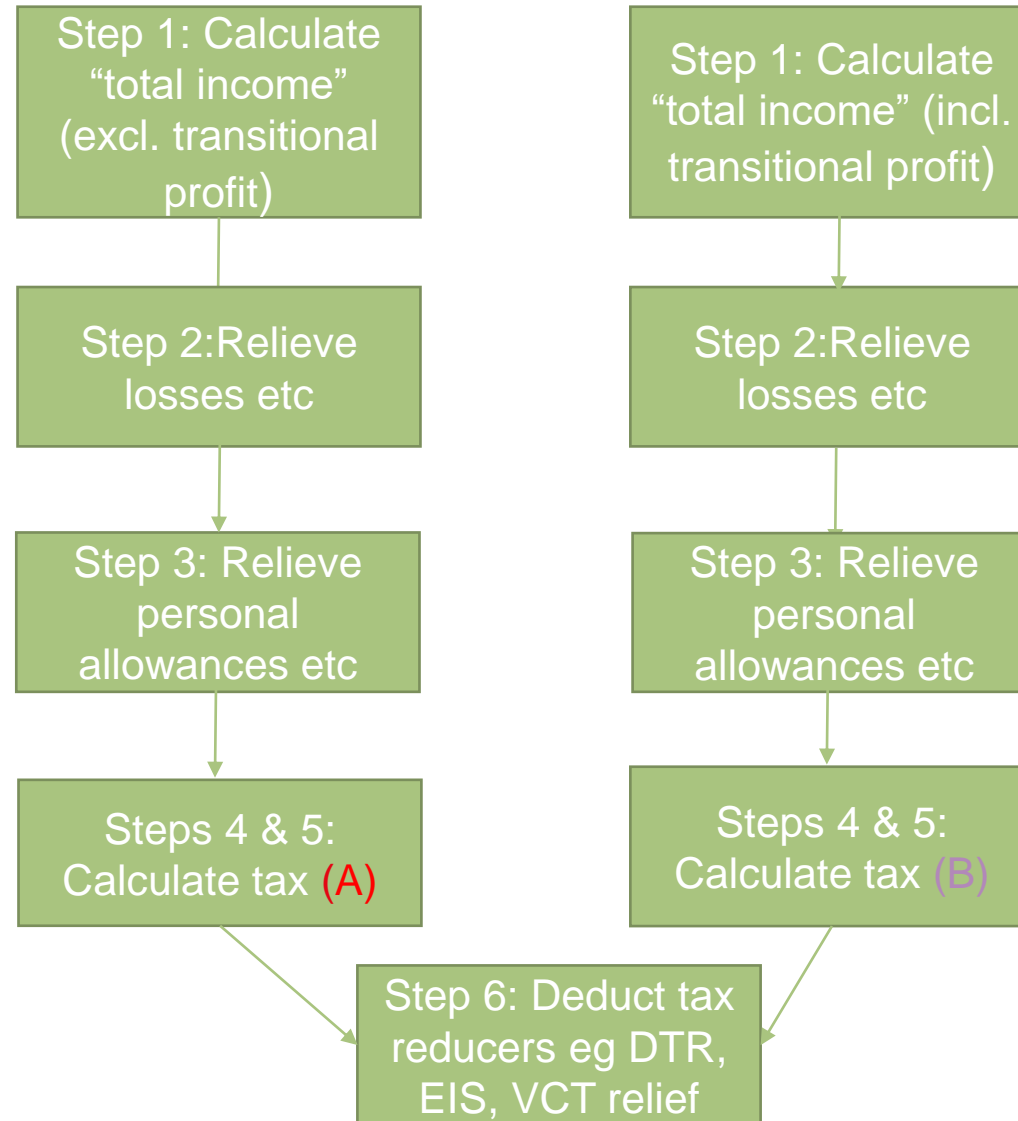
64	Net business profit for tax purposes (if box 47 + box 61 minus (box 48 + box 63) is positive)	£						8	0	0	0	.	0	0
65	Net business loss for tax purposes (if box 48 + box 63 minus (box 47 + box 61) is positive)	£										.	0	0
66	Date your basis period began DD MM YYYY		0	1	0	1	2	0	2	3				
67	Date your basis period ended DD MM YYYY		0	5	0	4	2	0	2	4				
68	If your basis period is not the same as your accounting period, enter the adjustment needed to arrive at the profit or loss for the basis period – if the adjustment needs to be taken off the profit figure, put a minus sign (-) in the box – do not include any transition profit or loss in this box, see box 73.1	£	-				2	4	0	0	0	.	0	0
73.1	Profit or loss of the transition part of the basis period	£	-				8	0	0	0	.	0	0	
73.2	Overlap relief used on the transition part of the basis period this year	£									.	0	0	

What about partnerships?

- Partnership return (SA800) is unchanged
 - Report profits for accounting periods ending in 2023/24
- Issue partnership statement to each partner
 - 2 statements in Scenario 3
- Copy figure to box 8 SA104F as normal
 - if 2 statements, copy the later figure only, do not aggregate
- Use box 9 to adjust box 8 figure to standard profit as before
- Transition profit in box 16.1

6	Date your basis period began DD MM YYYY	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>			
7	Date your basis period ended DD MM YYYY	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>			
8	Your share of the partnership's profit or loss - from box 11 or box 12 on the Partnership Statement	£	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	•	<input type="text"/>	<input type="text"/>
9	If your basis period is not the same as the partnership's accounting period, enter the adjustment needed to arrive at the profit or loss for your basis period – do not include any transition profit or loss in this box, see box 16.1	£	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	•	<input type="text"/>	<input type="text"/>
16.1	Profit or loss of the transition part of the basis period	£	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	•	<input type="text"/>	<input type="text"/>
16.2	Overlap relief used on the transition part of the basis period this year	£	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	•	<input type="text"/>	<input type="text"/>

Income tax calculation from 2023/24



Tax on transitional profit is
 $(B) - (A)$

Income tax calculation example

Jamie has the following results in 2023/24:

- Standard profits- £98,000
- Transition profits- £20,000 (divided by 5 = £4,000)
- Personal allowance £12,570

Income tax calculation example

Component of total income	Standard profits	Transition profits
Profits	£98,000	£4,000
Net income	£98,000	
Deduct personal allowance	$£98,000 - £12,570 =$ £85,430	
Calculate tax liability at 20% for the first £37,700 above the personal allowance	$£37,700 \times 20\% =$ £7,540	
Calculate tax liability at 40% for the remaining income	$£47,730 \times 40\% =$ £19,092	
Total tax liability	$£7,540 + £19,092 =$ £26,632 (A)	

Income tax calculation example

Component of total income	Standard profits	Transition profits
Profits	£98,000	£4,000
Net income	£102,000	
Deduct personal allowance	£102,000 - £11,570 = £90,430	
Calculate tax liability at 20% for the first £37,700 above the personal allowance	£37,700 x 20% = £7,540	
Calculate tax liability at 40% for the remaining income	£52,730 x 40% = £21,092	
Total tax liability	£7,540 + £21,092 = £28,632 (B)	

Tax on transitional profit is £2,000 (B – A), essentially chargeable at a marginal rate of 50% (£2k @ 40%, £2k @ 60%)

Total tax liability = £28,632

Which thresholds will be affected by transitional profits?

Yes	No
Student loan repayments	Tax credits and universal credits
	High Income Child Benefit Charge
UK relevant earnings for tax relief on pension contributions	Pensions annual allowance taper
Income tax payments on account	Capital gains tax rates

Averaging rules and transition profits

- General rule: Ignore the transition profits when working out the averaging, taxing them separately alongside the averaged profits

Example

A farmer has the following results (plus overlap relief of £5,000):

- 30 September 2022 - £10,000
- 30 September 2023 - £20,000
- 30 September 2024 - £40,000
- 30 September 2025 - £15,000

Averaging rules example

2022/23: Taxed on profits of £10,000

2023/24 (Transitional year):

y/e 30/9/2023

£20,000

6 mths of y/e 30/9/24

£20,000

Less: overlap relief

(£5,000)

£15,000

Spread over 5 years

£3,000 (ignored for averaging)

Averaged profits

(£20,000 + £10,000)/2 = £15,000

2023/24 result

£15,000 + £3,000 = £18,000

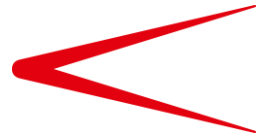
30/9/2022 - £10,000

30/9/2023 - £20,000

30/9/2024 - £40,000

30/9/2025 - £15,000

Overlap relief - £5,000



Questions

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