Tax Talk

Simplifying the complexities of Tax

March 2023

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MTD for ITSA – where are we now?

The government has further delayed the introduction of MTD for ITSA. The new timetable means it will be phased in from 6 April 2026. We consider the implications.

So who will be affected by this two-year postponement? Self-employed individuals and landlords with income exceeding £50,000 will need to join the MTD regime from 6 April 2026. Those with income between £30,000 and £50,000 will be required to join from 6 April 2027.

The government is currently reviewing whether smaller businesses with an income below £30,000 will be required to join at all.

We also now know MTD for ITSA will not be extended to general partnerships in 2025, as originally planned. But the government remains committed to introducing the regime to partnerships in the future.

HMRC has temporarily stopped adding any new entrants to its MTD for the ITSA pilot. No timeline has been released for when the pilot will reopen.

Where do we go from here?

We await further announcements on the pilot scheme and other communications about the regime. As soon as more information is available, we'll provide an update. In the meantime, for further detail on what the government planned, please see our previous articles on MTD for ITSA here.

What did we already know?

- Making Tax Digital for Income Tax Self Assessment (MTD for ITSA) is a new way of reporting property and self-employment income to HMRC. It will mean keeping digital records and sending Income Tax updates to HMRC quarterly.
- This will give an estimated calculation of the tax owed, which should help you set aside enough money to pay your annual tax bill.
- Payment dates will remain the same, with Income Tax due on 31 January and payments on account in January and July.
- At the end of the year, you will confirm your profits on an end of period statement (EOPS). This will include any tax or accounting adjustments and will finalise the tax position of each of your property and self-employment businesses.

  The EOPS will be filed by the normal Self Assessment deadline of 31 January following the relevant tax year.
- You will also need to submit a final declaration (which is the MTD equivalent of the current Self Assessment tax return), following your EOPS.

  This will bring together all business and personal information from the EOPS and information on non-MTD sources of income, in order to determine the final tax liability. The final declaration will also be filed by 31 January following the relevant tax year.
- If you receive income from more than one source, it is the total turnover from all sources of self-employment and property that counts towards your qualifying income for the purposes of MTD for ITSA.
- Until recently, MTD for ITSA was going to become mandatory from 6 April 2024 for individuals who had a turnover of more than £10,000 from their self-employment or property business. This is now under review (see above).
- HMRC is currently running a limited pilot of MTD for ITSA, allowing qualifying individuals to record their income and expenses using MTD compliant software and send quarterly income tax updates to HMRC.

If you have any questions, or think you will be affected by MTD for ITSA and need guidance on how to prepare, please contact Vardeep Kular.

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Share capital changes: what it means for your personal tax

When a company reorganises its shares, what is the impact for individual shareholders?

Commercial reorganisations, mergers and acquisitions are very common. Although there will be commercial decisions driving the restructuring, shareholders must consider the impact on their personal wider tax position.

The restructuring will often include a share for share exchange. So how does this affect shareholders?

What is a share for share exchange?

This is the process where a company exchanges or issues shares in consideration of the exchange or issues of shares in another company. In other words, the shareholders swap their shares in one company for shares in another or different shares in the same company.

There are special rules governing share for share exchanges. The main benefit of these rules is that, as a result of the exchange, the shareholders are not considered to have disposed of their original shareholding. This means the exchange doesn't trigger a dry tax charge on the shareholder. Instead, the new shares are deemed to 'stand in the shoes' of the original shareholding.

A company planning to carry out a share for share exchange transaction can apply to HMRC for clearance to confirm that the rules would apply.

Whilst the exchange itself may not trigger a disposal, it's important to consider if the reorganisation could have a wider effect on the individual shareholders' tax position.

Non-domiciled shareholders

In the Autumn statement, the government announced new anti-avoidance measures. These aimed to stop non-domiciled individuals from avoiding UK tax on chargeable gains made on the disposal of UK business, by taking advantage of the share for share rules.

These new rules apply to share for share exchanges or schemes of reconstruction after 17 November 2022. The measure only affects shareholders holding 5% or more of a close company.

The rules mean that shares received in a non-UK company in exchange for shares in a UK company, will continue to be treated as UK shares for Capital Gains Tax (CGT). Dividends will also remain in the scope of UK tax.

Although these rules are fairly esoteric, it's important that affected shareholders are aware of them. Whilst they will no longer own UK shares, the effect of these rules is to treat foreign shares as being UK. As such, they are outside the scope of the remittance basis.

These measures apply to Income Tax and CGT, so the exchange would still be effective for Inheritance Tax (IHT). But, as the UK shares would most likely have qualified for 100% business property relief, this is unlikely to be relevant.

Impact on Business Asset Disposal Relief

Business Asset Disposal Relief (BADR) reduces the rate charged on the first £1m of qualifying disposals from 20% to 10%. For BADR to apply, the shareholder must have owned more than 5% of the trading company, and be an officer or employer, for the 24 months leading up to disposal.

The share for share exchange rules will stop a taxable gain arising on the share swap. But the exchange could impact the availability of BADR in the future.

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For example, BADR might not be available on the new shares if, as a result of the exchange, the shareholder will own less than 5% of the new company or there will be a disposal within two years.

Because of this, it is possible to disapply the share for shares rules. The decision either way has to be made by 31 January following the end of the tax year of disposal.

Opting to disapply the share for share rules means:

- a gain will be calculated as if the value of the new shares received was cash. The gain will then qualify for BADR.
- the new shares will have a base cost equal to the market value at the date of takeover.

The effect is that the exchange is immediately taxable, but reduces the gain on a future disposal. So it's important to consider whether the election is appropriate.

Impact on SEIS and EIS

SEIS and EIS are advantages share schemes that provide Income Tax repayments equal to 50% or 30% respectively of the amount invested, and valuable exemptions from CGT.

Usually, if these shares are disposed of within three years, these reliefs are lost. As a share for share exchange counts as a disposal, it could result in the loss of these valuable reliefs.

There are rules which can allow the new holding to continue to qualify for relief. But strict requirements apply which are more onerous than the general share for share exchange rules.

In a nutshell:

- the new company must have no shareholders other than subscribers before the share exchange.
- the consideration for the old shares must consist wholly of the issue of the new shares in the new company.

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- the consideration for the new shares of each description must consist wholly of old shares of the corresponding description.
- HMRC must have confirmed in advance that CGT relief for the share exchange will not be disapplied on tax avoidance grounds.

In general, the continuation will apply where the shares are acquired by a new company and are the sole consideration. HMRC clearance should be obtained if EIS is applicable to some of the shares.

Impact on IHT

Shares in unquoted trading companies can qualify for relief from IHT at up to 100%. This is a very valuable relief.

To be eligible, the shares must be owned for the two years before death. But there are certain exceptions to the two-year ownership requirement for replacement business property. This will be apply if the property replaced other property that qualified for business property relief, and the combined period of ownership is at least two of the last five years.

What's more, where there's been a share for share exchange and the new shares would be identified with previously held qualifying shares, the owner may treat the period of ownership of the new shares as including that of the original shares.

When a company is undergoing a reorganisation, it's important that the individual shareholders take personal advice about the effect on their wider tax position. If you would like help with any of the issues raised in this article, please contact Stephen Kenny.

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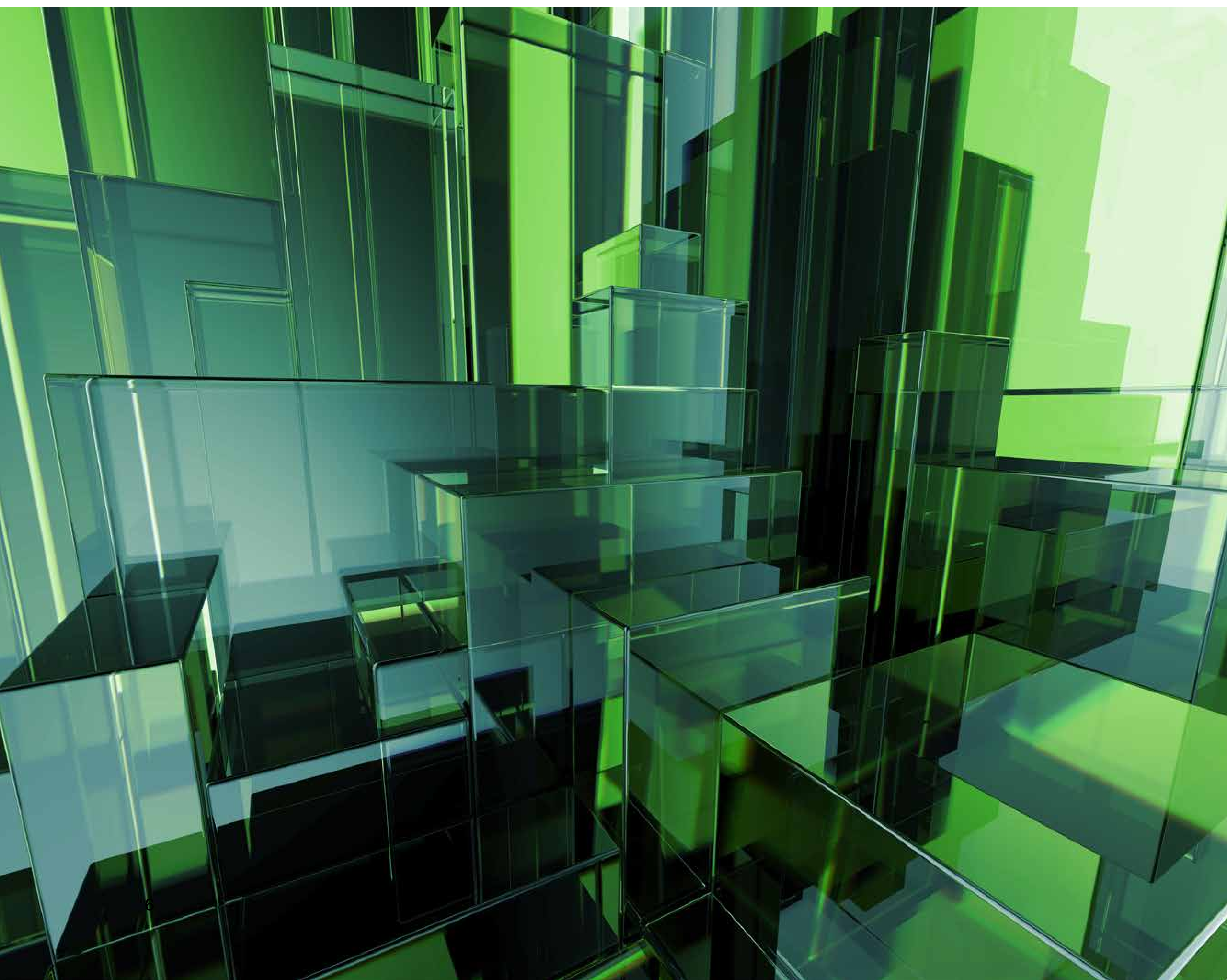
Recovery of VAT on deal fees

The VAT rules in relation to acquisitions are complex. We look at the recent Ince Gordon Dadds versus HMRC case to see how companies can be better prepared.



Businesses which make company acquisitions as part of their growth strategy often incur significant costs for due diligence and other professional fees. Recovery of VAT on these costs is not straightforward. In fact, it can lead to significant disputes between businesses and HMRC, sometimes ending in litigation. But there are ways of reducing the chance of an HMRC challenge to the recovery of this VAT. The key is to consider the position at the outset and take appropriate action.

Usually, legislation only permits the recovery of VAT where it is considered to be 'attributable' to taxable supplies. For VAT relating to company acquisitions HMRC takes the view that, for such VAT to be claimable, there needs to be a 'direct and immediate link' between the VAT costs incurred and the taxable supplies made.

Where a business simply acquires a company and then passively holds the acquired entity without any economic activity of its own, HMRC will usually rule that the VAT incurred on the costs of acquiring subsidiaries are not recoverable. This view will still apply even if the holding company joins a VAT group with the acquired companies.

Ince Gordon Dadds VAT case

The recent First-tier Tribunal (Tax) case of Ince Gordon Dadds LLP (IGD) highlights this issue. The FTT did not accept an appeal made by the company over HMRC's rejection of its claim for the recovery of VAT. This related to costs incurred by the acquirer Work Group plc (WG) on a fundraise it made for Ince Gordon's acquisition. Whilst bank or stockbroker charges for fundraising are typically exempt from VAT, WG incurred VAT on related accountancy, advisory and stock exchange fees.

Following acquisition, WG joined a VAT group with IGD and recovered the input VAT costs on the VAT group's subsequent VAT filing.

HMRC rejected the claim for VAT costs on the fundraise because it didn't believe there was a sufficient link between the costs incurred and the ongoing taxable activities of the VAT group.

HMRC said WG had not provided sufficient evidence to show it was engaged in economic activity at the relevant time. Whilst WG entered into a management services agreement (MSA) with IGD and other group entities, this did not happen until about two years post acquisition, although the MSA backdated supplies to the takeover date.

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Despite the existence of an MSA and associated invoice, HMRC didn't accept these as proof that WG had its own economic activity in supplying management services in return for payment - that was separate from any dividends received. What's more, HMRC noted that WG's accounts showed no services were provided to any of the group entities either at the time of, or after, the takeover.

View of the Tribunal

The Tribunal held that the input VAT costs incurred for the acquisition were not recoverable, and dismissed IGD's appeal.

It said that the burden of proof is on the claimant to show that the VAT costs are attributable to a taxable business activity. It held that where there are costs in relation to a fundraise for an acquisition, related input VAT is recoverable if the funds are used for a future taxable activity of that entity. In the case of an acquirer joining a VAT group with the acquired entity, this test is applied to the activities of the VAT group as a whole.

Despite this, the Tribunal said it was not persuaded that the MSA and associated invoice, both drawn up long after the event, demonstrated a taxable business activity by WG. It determined that the funds were to be used primarily for WG purchasing and holding new subsidiaries, rather than for the acquired company's management services. It therefore held that the input VAT was irrecoverable.

What actions can businesses take?

This ruling shows that an acquirer joining a VAT group with the acquired entity following an acquisition doesn't necessarily demonstrate the necessary link with the VAT costs incurred and future taxable supplies.

The decision highlights the importance of proving that the acquirer will be undertaking taxable economic activities post acquisition, and ideally showing this intention at the outset. Entering into an MSA between the acquirer and acquiree at the time of the acquisition can help to demonstrate this.

If an MSA is drawn up at a later date, and/or if the corresponding charges under the MSA are not made, this makes it more difficult to establish the link between the VAT costs on the acquisition and the subsequent taxable management services.

It's important to consider each case on its own merits to see whether a business is able to recover the VAT incurred on transactional fees and the related VAT implications.

If you would like advice and support on any issues raised in this article, please contact Nadav Shayovitz.

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We offer comprehensive tax compliance and advisory services to a range of clients, both in the UK and globally, helping them find their way in the increasingly complex world of tax.

We find practical solutions that we use to our clients’ advantage. Our team of experts supports individuals, and businesses ranging from start-ups and SMEs to large international groups, both listed and privately owned.

Where understanding of our clients’ sector makes the difference, our experts invest their in-depth industry expertise to provide invaluable support and insights.

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Our Business Tax team will ensure that you are both tax compliant and efficient.

We provide specialist corporate and business tax advice on both a local and international level, which includes senior accounting officer and large business compliance, transaction services, due diligence, R&D tax relief, employer solutions and global mobility. We also support both the personal and business affairs of partnerships and LLPs.

Read more

Personal tax and wealth management

Our team will guide you through the complex world of taxes, helping you meet all filing requirements and identifying risks and opportunities to help mitigate tax liabilities.

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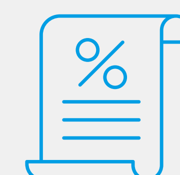

VAT and Indirect taxes

Our indirect tax team will support you in meeting your VAT compliance objectives and advise you on any VAT issues that your business faces.

We can ensure that your VAT risk is assessed and managed, and that your VAT recovery is optimised. We can also provide advice and compliance services on other indirect taxes, such as Insurance Premium Tax, Customs duty, and Air Passenger Duty.

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Tax disputes

HMRC is increasing the number and scope of tax investigations into both individuals and businesses, covering all aspects of potential underpayments of tax, including offshore investments, personal and corporate Self Assessment Tax Returns, PAYE and NIC compliance and VAT.

If an issue arises, our trusted advisors will match the right specialists with your needs to provide you the necessary support – whether for a routine HMRC enquiry or a more complex investigation.

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