
# Basis Period Reform

**From the tax year 2024-25, self-employed businesses and partners in trading partnerships will be taxed on the profits arising in the tax year itself, regardless of their accounting year end.**

**The tax year 2023-24 will be a transitional year, when taxpayers must move from the current rules to the new basis of assessment.**

## Why the change?

HMRC are moving away from the ‘current year’ basis of taxation to a ‘tax year’ basis of assessment to create a more transparent set of rules for the allocation of trading income to tax years. The basis period rules, particularly overlap profits and overlap relief, are confusing and many businesses eligible for relief are not claiming it - the changes look to remove these complications and ensure the appropriate relief is claimed.

## The impact on businesses and partnerships

According to HMRC, 93% of self-employed businesses and 68% of partners are already on the tax year basis so will see no significant change in how profits are reported.

Sole traders and partnerships that do not have an accounting year between 31 March and 5 April will be affected by the changes. Businesses may encounter additional administrative costs and cash flow implications, as some profits will be taxable earlier than previously would have been the case.

Businesses that do not currently align to the tax year for their accounts will have to apportion figures from more than one set of accounts to calculate the taxable profit for the year.

The requirement to pay income tax based on the profits earned during the tax year does not mean businesses have to change their accounting date - it is just a change in the way profits are calculated. Some businesses may choose to change their accounting date to simplify reporting going forwards, but this might not always be a viable option for commercial or reporting reasons.

## Late accounting date rules

Where a business has an accounting date that falls between 31 March and 4 April, the profits for the days after the accounting date, up to including 5 April, are treated as if they arise in the following tax year. There is no need to make really small apportionments to match the accounts up to 5 April.

## Transition year

The 2023-24 tax year is the year for all sole traders and partnerships with non-tax year basis periods to align them with the tax year, making sure profits are taxed appropriately and all their overlap relief is used.

All businesses will have their basis period determined by a set of special rules in 2023-24.

These rules consist of 2 components, depending on the circumstances of the business:

1. The standard part, the first 12 months of the basis period; and
2. The transition part, running from the end of the standard part to 5 April or a late accounting date (if this falls on 31 March to 4 April inclusive).

A business with an accounting end date of 31 December would have a basis period for 2023-24 that was made up of:

1. The standard part of 1 January - 31 December 2023; and
2. The transition part of 1 January - 5 April 2024.

## Transition profit

After calculating the profits arising in the transition part of the basis period, and deducting any available overlap relief, there may be an amount of 'transition profit'.

This transition profit will be spread by default across 5 years, starting in the transition year.

For each of the first 4 tax years, 20% of the amount of the profits will be treated as arising in each year starting with the 2023-24 tax year. The balance of profits will be treated as arising in the 5th tax year (2027-28).

The taxpayer can elect to accelerate the amount of transition profits brought into account in any one tax year. They may wish to do this if, for example, other income is lower in the year, meaning more basic rate band is available. Any remaining transition profits will then be spread equally over the remaining spreading period, subject to any further acceleration of profits.

Please note: There are also special rules if there are losses in the standard part of the calculation or transition part.

## Overlap relief

Businesses with non-tax year aligned accounts will have experienced overlapping basis periods at some point in their history. If they were making profits at that point, they will have been taxed twice on those profits and generated a related amount of overlap relief.

Overlap relief is normally carried forward until there is a change in accounting date or the business ceases to trade. The relief can then be used as a deduction against profits.

The move to a tax year basis in 2023-24, means overlap relief no longer has to be carried forward, everyone can use it as a deduction against trading profits.

**Businesses will not be able to use any outstanding overlap relief after 2023-24.**

## Provisional figures

There may be some sole traders and partnerships with accounting year ends late in the year that may not be able to finalise their accounts before the tax return deadline.

It may be necessary for these businesses to submit a return with provisional figures and then amend these at a later stage.

## Preparing for the change

Sole traders and partnerships not already using the tax year basis should familiarise themselves with the implications of basis period reform.

Taking professional advice and planning ahead for the changes enables businesses to navigate any negative impact on cashflow or future tax position.


## How M+A Partners can help

For any queries on basis period reform and how to prepare for all profits being taxable in the tax year in which they arise, please get in touch with your usual **M+A Partners** adviser or contact our experts.

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