The Bar Council

Taxation and retirement benefits handbook

Tenth edition

Preface

It is six years since the previous edition of the Bar Council's *Taxation and Retirement Benefits Handbook* (the 'Handbook') was published. Every chapter has been updated for this Tenth Edition. It has been written by the Taxation Panel of the Bar Council's Remuneration Committee.

Panel members have given their time pro bono and the Bar Council is very grateful for their contributions:

Richard Vallat QC	Pump Court Tax Chambers (Chair)
Barrie Akin	Devereux Chambers
Nick Avis	Place Campbell Chartered Accountants
Nick Brennan	Citroen Wells Chartered Accountants
Harriet Brown	Old Square Tax Chambers
Felicity Cullen QC	Devereux Chambers
David Marks	Citroen Wells Chartered Accountants
Mark Watkins	Place Campbell Chartered Accountants
Adrian Vincent	Bar Council (Executive)

We are also grateful to Kevin Harms at Place Campbell Close Brothers Ltd for his input into Part Nine.

The Handbook is intended to provide practical assistance to barristers across the whole span of their professional life, beginning from pupillage, through to retirement and making a will. It is particularly focussed to help self-employed barristers, who by the nature of self-employment have more complex tax arrangements than employed barristers. The Handbook does not constitute tax or legal advice and the Bar Council does not accept any liability in law for any loss or damage however caused.

Self-employed barristers may find it convenient to employ an accountant to help manage their tax responsibilities. Barristers should not, however, leave everything to their accountant. Tax matters can overlap with a barrister's regulatory responsibilities, and not every accountant is an expert in the Legal Services Act or the role of the Bar Standards Board. For example, I received a call from a self-employed barrister who, on the recommendation of his accountant, had recently set up a limited company through which he intended to supply his legal services. I asked the barrister whether his new company was regulated by the BSB to provide legal services, and whether he had applied to the BSB to change from a self-employed to an employed or Dual Capacity practising certificate? Such implications had not occurred to the barrister. I therefore drew his attention to Part Ten of the Handbook, and the "Entities" document on the Bar Council's Ethics and Practice website: www.barcouncilethics.co.uk

This cautionary tale illustrates the need for a relationship of teamwork between barrister and accountant.

Adrian Vincent
Head of Policy: Legal Practice and Remuneration, Bar Council.
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For further information please contact
The General Council of the Bar of England and Wales
289-293 High Holborn, London WC1V 7HZ
Email: Remuneration@barcouncil.org.uk

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Part One: Income Tax

1. This part is concerned with the taxation of self-employed barristers' income. It covers how that income is quantified for tax purposes and what deductions are allowed.

Income tax for barristers

2. The income of a self-employed barrister is professional income and is taxed on the basis of accounting periods (or periods of account).

3. For income tax purposes income is divided into different categories: notably trading, professional, employment and investment income. Different tax rates and rules may apply in establishing the income to be returned. Furthermore, different deductions may be allowed before the income is taxed and the set-off of losses and allowances may be different. Also, the impact of National Insurance Contributions (NIC) will depend upon the type of income.

4. Income tax is charged on the income for a particular year of assessment (or "tax year"). For individuals the year of assessment runs from 6 April one year to 5 April the next. For some types of income (e.g., interest and dividends), the income for a given year of assessment is simply the income received in that year. For professional income, however, the income for a year of assessment is generally the income for the accounting period ending in that year and the accounting period is generally a year ending with the date in respect of which the taxpayer draws up the accounts. For example, a barrister drawing up accounts to 31 March each year would pay tax on their professional income for the accounting period ending 31 March 2021 in the tax year ending 5th April 2021 (referred to as tax year 2020/2021) and would therefore be required to include that income in their return to be filed by 31 January 2022. A barrister drawing up accounts to 30 April each year would pay tax on their professional income for the accounting period ending 30 April 2021 in the tax year 2021/2022 (which runs from 6 April 2021 to 5 April 2022) and include this income in their return filed by 31 January 2023.

5. The Government proposes to end the 'Current Year Basis' of assessment and move to 'Tax Year' basis with effect from 2024/25 with 2023/24 being a transitional year. See paragraph 64.

6. Returns of income and capital gains tax can be made in paper form (non-electronic return) or online (electronic return). Returns must be made by the filing date. A non-electronic return must be made on or before 31 October following the tax year to which it relates. An electronic return must be made on or before 31 January

following the tax year to which it relates. From 6 April 2024, Making Tax Digital for income tax is to be introduced which will result in a major change in the filing obligations. This is discussed further in paragraphs 62 to 63 below.

7. The electronic tax return is called a self-assessment return and must include a calculation of the liability to tax on the income and capital gains included in the return (such calculation generally being carried out by the relevant tax return software). Her Majesty's Revenue and Customs (HMRC) will calculate the liability where a paper return is made within the time limits.

8. Tax due under self-assessment is payable as follows:

   a. On 31 January during the tax year and on 31 July after the end of the tax year, the taxpayer must make a payment on account. Each payment is generally half the tax due for the previous year, and

   b. On 31 January after the end of the tax year, the taxpayer must make a balancing payment or, where the payments on account exceed the liability, claim a repayment.

9. There is further detail on self-assessment in Part Eight of this guidance.

10. Thus, a barrister will need to pay[1]:

   a. Balancing payment of tax for **previous** year of assessment (tax year 2020/2021) on 31 January 2022,

   b. First instalment of tax for **current** tax year ending on 5 April 2022 (year 2021/2022) on 31 January 2022, and

   c. Second instalment of tax for the current tax year ending on 5 April 2021 (tax year 2021/2022) on 31 July 2022.

11. The sequence of events for payment of income tax for the tax year 2021/2022 is:

Date	Event
6 April 2021	Tax year 2021/2022 begins

[1] Any temporary changes to timing of payment obligations arising from Covid-19 measures of relief have been disregarded, and specific advice should be taken on the current position and any conditions or claims involved in seeking such relief as is available.

31 July 2021	2nd instalment payment for tax for 2020/2021
31 October 2021	2020/2021 filing date for paper returns
31 January 2022	Filing date for electronic tax returns for tax year 2020/2021
31 January 2022	Balancing payment (or credit) for tax underpaid (overpaid) by instalments for 2020/21for 20/21 and
31 January 2022	1st instalment payment for tax year 2021/22
5 April 2022	Tax year 2021/2022 ends
6 April 2022	Tax year 2021/2022 commences
31 July 2022	2nd instalment payment for tax year 2021/2022
31 October 2022	Filing date for paper returns for tax year 2021/2022
31 January 2023	Filing date for electronic returns for tax year 2020/2021
31 January 2023	Balancing payment (or credit) for tax underpaid (overpaid) by instalments for 2021/2022
31 January 2023	1st instalment payment for tax 2022/2023

12. If no return (or no notice to complete a return) is issued, a taxpayer in receipt of taxable income must notify HMRC by 5 October after the year of assessment in which the income is received. Therefore, a taxpayer in receipt of taxable income in the year ended 5 April 2022 who does not receive a return from HMRC must notify them by 5 October 2022.

13. Returning to the examples given above, it can be seen that with an accounting period ending early in the year of assessment there is a greater deferral of payment of the related tax liability on those earnings compared with an accounting period ending later in the year. Consider a fee earned in March 2021. The barrister drawing up accounts to 31 March would pay tax on that fee in tax year 2020/21 whereas the

barrister drawing up accounts to 30 April would pay tax on that fee in tax year 2021/2022 (i.e. a year later). Broadly, taxpayers are free to choose when their accounting periods end. There are other factors to consider that may influence this decision (which are outside the scope of this guidance). These are important decisions and it might be sensible to seek advice from members of chambers who have recently had to consider these questions themselves or an accountant knowledgeable in the tax and accounting of practising at the Bar. But bear in mind that 'Tax year' basis is set to apply from 2023/24 (see paragraph 5) and a 31 March or 5 April year end may then be appropriate. There are anti-avoidance provisions to prevent tax advantage being obtained by repeatedly changing accounting dates. Special rules apply to calculate how profits are taxed in the first years of practice.

14. A barrister's profits may be computed in one of two ways, as follows:

a. **The earnings basis** in accordance with Generally Accepted Accounting Principles (GAAP). In essence, barristers are taxed on the billable value of their work done, whether or not paid (and even whether or not billed) and expenditure is relieved when incurred, whether or not settled, by the end of the accounting period.

b. **The cash basis**. The Finance Act 2013 introduced a new basis of cash accounting available to most unincorporated businesses, which includes barristers. It applies from the tax year 2013/14 onwards and has its own special set of rules which are discussed in paragraphs 38 and 39.

15. As well as fees received (if on the cash basis) earned income would include any other profits which the barrister derives from their profession; for example, income as royalties or commissions for books and articles and fees for acting as an arbitrator. Salaries for teaching law and from part-time judicial appointments are employment income and included in the return, though Pay As You Earn (PAYE) income tax will normally have been deducted from such payments. Certain other types of income, such as that from investments, are taxed in the year of assessment in which the income arises. For example, if a barrister's accounts are drawn up to 30 June each year and in addition they hold some shares and receive bank interest, the tax return for the fiscal year 2021/2022 would include:

a. Taxable profits from the Bar from 1 July 2020 to 30 June 2021

b. Fees for sitting as a Recorder between 6 April 2021 and 5 April 2022, and

c. Share dividends and bank interest received between 6 April 2021 and 5 April 2022.

16. Except for tax withheld at source, the tax on all this income will be payable at the same time in accordance with the self-assessment regime.

Expenses

17. For expenditure to be deducted from income for tax purposes, it must be:

a. of a revenue nature and
b. incurred wholly and exclusively for the purposes of the profession.

18. There are also some specific statutory restrictions, for example a deduction for entertaining defined as hospitality of any kind is prohibited.

Capital or revenue expenditure

19. The category into which expenditure falls will depend on the precise facts of the expenditure in question. As a general rule, an expense which is incurred repeatedly would tend to be regarded as revenue whereas an expense incurred as a one off would tend to be capital. For example, lease payments for the rental of equipment would be regarded as revenue expenses but the purchase of the equipment outright would be treated as capital.

20. Generally, the following will be regarded as revenue expenses:

- Stationery
- Repairs
- Professional fees
- Telephone charges (line rental and call charges)
- Broadband
- Off street parking
- Hotels
- Travel
- Library and periodical subscriptions
- Devilling fees
- Robing room fees
- Chambers' rent
- Professional indemnity insurance premiums
- Bank charges
- Overdraft and loan interest used to fund business expenditure [2]
- Bar Council subscriptions
- Circuit subscriptions

[2] But not to fund drawings in excess of profits.

- Specialist Bar Association subscriptions
- Other professional association subscriptions
- Staff costs
- Equipment rental (e.g., computer leasing)
- Law report subscriptions
- Silk application and award fees
- Software licence where the useful economic life of the software is less than two years, and
- Website expenditure.

21. The following will be capital, if purchased and not rented:

- Furniture
- Sets of law reports
- Computers, peripheral equipment, and initial purchase of software
- Wigs and gowns, and
- Cars.

22. HMRC have issued a Capital v Revenue Expenditure Toolkit, accessible on HMRC's website[3], which gives guidance on the application of the distinction.

Wholly and exclusively

23. Not all revenue expenditure is deductible. The main test is that the expense be incurred "wholly and exclusively" for the purposes of the profession. It is specifically provided that if an expense is incurred for a dual purpose, that expense may be apportioned between any identifiable part or any identifiable proportion incurred wholly and exclusively for the purposes of the trade, and the part or proportion of the expense incurred for a non-business purpose. If the barrister works at home, they can claim a proportion of domestic expenses as the costs of maintaining an office at home. Traditionally this was undertaken by reference to the floor area of study compared with the floor area of whole dwelling. However, HMRC guidance does now allow the costs of a room at home, after apportioning total costs based on floor area, to be split between business and private use based on time spent in that room.[4] Likewise, if a barrister uses his or her car partly for business, a proportion of the running costs may be claimed as a business expense and this is usually calculated by reference to the business mileage as a percentage of total mileage.

[3] https://www.gov.uk/government/publications/hmrc-capital-vs-revenue-expenditure-toolkit

[4] See https://www.gov.uk/hmrc-internal-manuals/business-income-manual/bim47825 in particular example 4

24. In many cases it should be clear whether a cost is incurred for professional or personal reasons. Difficulties arise where the barrister has a dual purpose in incurring the expense, and it does not lend itself to apportionment between business and non-business use. In that case the expense is non-deductible in its entirety. The situations in which this rule applies include:

a. **Subsistence**: subsistence when in chambers is not deductible (although the costs of modest expenditure on subsistence away from chambers and home should be allowable, along with costs of accommodation, travel etc.).

b. **The cost of court clothing**: following the decision of the House of Lords in *Mallalieu v Drummond*[5], the cost of court clothing, including dark suits and court shirts, is not allowed as a deduction, since the barrister is said to be wearing these clothes partly for the personal reasons of modesty and warmth. This analysis should not extend to collars, bands and studs, or laundry costs of the same (as indicated above, the costs of wigs and gowns are capital so cannot be deducted in any event), and

c. **Dining expenses:** HMRC takes the view that the social element of dining is inseparable from the professional.

Travel and motor expenses

25. The cost of travel between a barrister's home and chambers (and associated costs such as that of a parking space) is generally not allowable. In rare cases, the barrister may be able to demonstrate that their work base is the home rather than chambers so that all travel expenditure from home for professional purposes would be allowable. The costs of travelling from home or chambers direct to Court and between Courts are generally allowable deductions in practice.

26. The treatment of motor expenses generally follows that of travelling as above with the same restriction on deduction for travel between home and chambers.

27. As it is often difficult to determine the percentage of total motoring costs that relate to business, taxpayers are encouraged to keep a log of business mileage and establish the appropriate percentage. In certain circumstances reasonable estimates might be accepted.

28. As an alternative, barristers may wish to keep a log of their business mileage and claim at the statutorily fixed rate of 45p per mile for up to 10,000 business miles each

[5] See *Mallalieu v Drummond* [1983] AC 861.

year and 25p per mile in excess of that. From the tax year 2013/14 to 2022/2023[6] these rates have statutory authority to be used when preparing self-employed accounts. The use of these rates precludes a separate claim for tax relief (in the form of capital allowances) on the cost of the car itself.

Use of Home as Office/Study

29. For use of home as an office/study, barristers can opt to claim a statutorily fixed rate deduction from the tax year 2013/14 onwards[7]), in substitution of the actual (apportioned) expenditure. The deduction is calculated by reference to the number of hours worked at home in a month as follows:

Number of hours worked	*Applicable amount*
25 or more	*£10*
51 or more	*£18*
101 or more	*£26*

The total fixed deduction for a year is the sum of the monthly amounts. This calculation assumes, of course, detailed record-keeping of hours worked at home.

Capital allowances

30. Allowances are given for capital expenditure incurred wholly and exclusively for the purposes of the profession. These are "capital allowances" and are discussed further in Part Four. Essentially, a proportion of the capital expenditure, known as the Annual Investment Allowance (AIA) or Writing Down Allowance (WDA) is allowed as a deduction from income each year as if it were a revenue expense.

31. Under the cash basis, with the exception of cars, capital expenditure (which would otherwise be eligible for capital allowances) is immediately deductible against income when paid.

Calculation of profits

32. The tax rules on the calculation of barristers' profits for income tax purposes are largely set out in the Income Tax (Trading and Other Income) Act 2005 (ITTOIA).

[6] See Section 94F *Income Tax (Trading and Other Income) Act 2005* ["ITTOIA"]

[7] See Section 94H ITTOIA 2005

33. Barristers in self-employed practice who are UK resident in a tax year are carrying on a profession and are charged to income tax on the "full amount of the profits of the tax year."[8]

34. Two questions arise:

a. what are the profits of the tax year?, and
b. what is the full amount of the profits?

35. The tax year runs from 6 April to the following 5 April. The profits of the tax year are the profits for the accounting period which ends in the tax year. As noted above, a barrister can choose which accounting period to use.

Accounting period	Tax year
6 April 2021to 5 April 2022	2021/2022
1 May 2021to 30 April 2022	2022/2023
1 January 2022 to 31 December 2022	2022/2023

36. It follows that the barrister commencing professional practice must decide what accounting period to use. Those already in practice may wish to change their accounting date at some future point in time for tax planning or for other reasons. But anti-avoidance rules may apply which prevent a change more than once every five years unless the change brings the accounting year end close to the end of the tax year.

Commencement of practice

37. Commencement of practice at the Bar starts from the beginning of the second six months of pupillage. This is discussed further in Part Two.

The cash basis

38. From the tax year 2013/14 onwards, barristers have the option of using the cash basis of accounting. A barrister's eligibility to use the cash basis includes an assessment of entry and exit thresholds based on the level of receipts. It is recommended that a barrister applying this basis of accounting read the HMRC guidance to confirm their eligibility to use it.

39. The principal features of the cash basis are:

[8] See section 5(8) of the Income Tax (Trading and Other Income) Act 2005.

a. It can be joined where receipts for the accounting year of assessment do not exceed £150,000 (or the pro-rated equivalent where the accounting period is less than a year). This figure applies for 2017/18 and subsequent years.[9]

b. Receipts are all "professional receipts" together with those from asset disposals to the extent that tax relief was claimed on such business capital expenditure previously.

c. Entry into the cash basis requires an election being made in the first tax return for which it applies. Tax returns from 2013/14 onwards include a box to tick for this purpose.

d. Where receipts for an accounting period exceed £300,000 [10], it is mandatory to leave the new cash basis for the earnings basis when preparing the next set of accounts, unless receipts in the subsequent accounting period fall back below the entry threshold of £150,000

e. If a barrister is VAT registered, the VAT may be dealt with either by excluding it altogether or by including it on a VAT-inclusive gross receipts and payments basis. If the latter is chosen, VAT payments to HMRC will be treated as an expense when paid and VAT repayments as a taxable receipt. If VAT is accounted for in this way, then the gross receipts plus VAT repayments count towards the entry and exit limits.

f. Interest charges on business borrowings are restricted to a £500 deduction.

g. The general treatment for capital expenditure, with the exception of cars, is that the expenditure is deductible when paid where it would otherwise qualify for capital allowances

h. Expenditure on cars can be calculated by reference to existing capital allowances and expenditure on actual running costs rules or alternatively, the fixed mileage rates can be used as discussed at paragraphs 23-28 above.

i. Losses can only be carried forward for relief against future profits as a barrister. Special rules apply on retirement (see Part Four).

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[9] See Section 31B(5)(a) ITTOIA 2005

[10] Strictly the figure is the greater of £300,000 and twice the VAT threshold, but as the VAT threshold from 1st April 2017 has been £85,000, the £300,000 will invariably exceed the £170,000 representing twice the VAT threshold. HMRC state simply "You can stay in the scheme up to a total business turnover of £300,000 per year. Above that, you'll need to use traditional accounting for your next tax return."

j. The cash basis may only be exited early if there is a change in commercial circumstances and by making a formal election to that effect. There must be an objective change of circumstances relating to the profession which makes an earnings basis more appropriate. Two of the examples given by HMRC are where more than £500 in interest deductions are being incurred and losses are suffered which the taxpayer wishes to relieve against other sources of income.

k. Leaving the cash basis for the earnings basis may give rise to 'adjustment income', a special form of relief to ameliorate the effect of the change. This is dealt with in paragraph 60 below.

l. There are also relieving provisions when a business changes from an earnings basis to a cash basis to avoid double counting. This is dealt with in paragraphs 58 to 59 below.

Earnings basis

40. The profits for a tax year are the profits earned in that year. Once use of the old or cash basis has to be discontinued, "full profits" means the profits calculated in accordance with Generally Accepted Accounting Principles (GAAP).[11]

41. Accounting practice requires the following:

a. Profits are the profits earned for the year, not cash received in the year.
b. A net increase in debtors (closing debtors minus opening debtors) constitutes income, which must be included in profits. A net decrease will conversely be a reduction in income and hence will reduce profits.
c. Deductible expenses are expenses incurred in the year, not expenses paid in the year.
d. Capital expenditure (e.g., purchase of computer or furniture) is non-deductible.

42. As regards the format of accounts, "profits" will consist of:

Fees received in year	x
Devilling fees	x
Debtors at year end (billed)	x
Complete and incomplete work at year end (unbilled)	x
Less:	

[11] See section 25(1) of the Income Tax (Trading and Other Income) Act 2005.

Opening debtors (billed)	x
Opening complete and incomplete work (unbilled)	(x)
Gross profit	x

43. For completed work at year end, a barrister has to bring in the fee that is reasonably expected to be received (whether or not billed). For incomplete work, the barrister must make a reasonable assessment of the amount earned so far.

Particular situations

Conditional Fee Agreements and Damages Based Agreements

44. In the case of agreements where payment is contingent on outcome, no right to consideration arises until the contingency occurs (i.e., the case is won). In those circumstances, no amount will generally be brought into account until the result of the case is known.

45. For those barristers who perform a high volume of contingent fee work, there may be scope to deem the contingency as reliably estimated on events not passed at the end of the accounting year, based on a track record over time of similar outcomes. However, this will require a significant amount of judgement and it is recommended expert advice be taken in considering this further. As this approach accelerates the income recognition with associated tax consequences, it is expected that this approach will rarely be employed.

Pay at end

46. Where there is no fixed fee, but payment is to be made when work is completed, an estimate of the fee earned up to the accounting date should be made.

Fixed fees

47. In the case of fixed fees, it should be possible to quantify "work in progress" at year end but the simpler course is to complete the piece of work and transfer "work in progress" to debtors.

Legal Aid

48. In legal aid cases "work in progress" should be recognised as it is done, not as payments on account are received. Allowance should also be made for the fact that some amounts may have to be repaid.

Legal aid Crown Court defence work

49. Under the Advocates Graduated Fee Scheme (AGFS), the Legal Aid Agency pay the entire advocacy fee for the case to the "Instructed Advocate" who is the advocate who undertook the trial. Out of that fee, the Instructed Advocate is responsible for paying any other advocates who covered hearings in that case ("Substitute Advocates"). Fees for the barrister who is the Instructed Advocate are generally paid into a chambers fee account,[12] from which the proportion of the fee owing to any Substitute Advocates is distributed. The Instructed Advocate should treat the Substitute Advocate as a sub-contractor. For example, if the fee is £200, the Instructed Advocate will treat the full amount as their income. If the fee is split £80 as to the Instructed Advocate, and £120 to the Substitute Advocate, the income of the Instructed Advocate remains £200. However, they will bring in as an expense the payment of £120 plus Value Added Tax (VAT) to the Substitute Advocate.

50. It should be noted that in practice most chambers operate a computerised system for recording these fees. The payment to the Substitute Advocate is usually entered on to the system as a reduction in the fee income of the Instructed Advocate.

Bad debts

51. Where an amount included in debtors at the year-end is unlikely be paid or paid in full, the difference between the amount included in debtors and the amount received or likely to be received is a bad debt. Tax relief is granted for bad debts because they are deductible from income.

52. There are two methods of recognising bad debts:

a. direct write-off method, or
b. allowance method.

53. Under the direct write-off method, the bad debt is recognised in the year in which it becomes uncollectable.

Example

Geoff has an accounting period ending on 31 March issued a fee note to a solicitor for £5,000 in the year to 31 March 2022. The fee had not been received at year end, so it was included in closing debtors of £40,000, and he paid tax on the amount in question.

[12] See Annex D of the Bar Council's "Graduated Fee Payment Protocol" https://www.barcouncilethics.co.uk/documents/graduated-fee-payment-protocol/

In the year to 31 March 2023, he agrees to reduce the fee to £2,500 because the solicitor has not been able to collect the money from the lay client. At 31 March 2023 his debtors (ignoring this case) are £50,000.

The fees received figure is increased by the full £10,000 change in debtors and two accounting entries are made to account for the bad debt:

Closing debtors are reduced by £2,500 and

Deductible expenses for the year 31 March 2023 are increased by £2,500.

This makes good the over-payment of tax for the year to 31 March 2022.

The loss is only expensed a year after the income had been recognised. Geoff could have avoided the time lag if it had been possible to recognise the bad debt when drawing up his accounts for the year to 31 March 2022.

54. To avoid the time lag, and in situations where bad debts are a recurrent feature of a practice, the allowance method should be used. At the year-end an estimate of uncollectable amounts is made, and an adjustment is made to closing debtors in the accounts for that year.

Using the figures in the above example, the following adjustment is made to fees received:

(Closing debtors – opening debtors) = (50,000 – 2,500) – 40,000 = 7,500

The need for a separate bad debt expense is removed and is therefore not shown.

55. If an amount which has been written off as a bad debt is subsequently recovered, it is simply included in the fees received for the accounting period in which it is received. This reverses the bad debt and restores the original income and taxation position.

Change from 'old' cash basis to earnings basis

56. An 'old' cash basis (with different rules to the cash basis referred to in the rest of this part of the Handbook) is largely of historical interest only, having been repealed in 2013 with transitional relief for those already on it limited to seven years from their first entering practice, but brief details are given here. By the end of their seventh year of practice, barristers on the 'old' cash basis must (if they have not made the change earlier) ascertain their debtors and "work in progress" at the last year end accounting date falling in the seventh year. This amount will constitute "adjustment income". Their accounts for year eight of practice will need to bring in closing debtors and

"work in progress" at full value, with opening amounts as at the end of year seven deductible. The opening debtors and "work in progress" are separately brought into charge to tax as adjustment income. (See also paragraph 91).

57. Adjustment income is income for tax and pension purposes, but not for National Insurance Contributions purposes. The tax charge on adjustment income arising on cessation of the cash basis can be spread over ten years (in contrast to six years under the 'new' cash basis explained at paragraph 60). Instalments for the first nine years are the lower of one-tenth of the catch-up charge or 10% of the barrister's pre-capital allowance profits. In the tenth year, the balance is brought into account. A barrister can elect to accelerate taxation of the catch-up charge. Any barrister in this position should take specific advice on calculations and adjustment income.

Change from earnings basis to cash basis

58. Where a barrister moves from the earnings basis to the ('new') cash basis, the closing debtors and work in progress (as computed under the earnings basis) are treated as deductions in the first accounts prepared under the cash basis. This is necessary to avoid double counting of income and expenses, initially under the earnings basis and again later as a receipt or payment under the cash basis.

59. Except for cars, any residual unrelieved capital allowances pools may be deducted as an expense in the first year under the cash basis provided that the expenditure has been fully paid for. Otherwise, a restriction applies with the unpaid portion deducted as an expense when paid

Examples

> *Juliette is currently on the earnings basis with a catch-up charge. She can switch to the cash basis provided that her receipts are below the £150,000 entry level. However, she should bear in mind that to the extent that her profits in the year prior to the change include debtors and work in progress (WIP) that have been taxed as earnings, the related receipts coming through in subsequent periods are not taxed again and an appropriate adjustment should be made to prevent duplication. If she is within the period to which she is assessed on the catch-up, that is generally the ten years following her first seven years, that will continue until it has all been assessed. It is important to remember that even though Juliette has elected to transfer to the cash basis from an earnings basis whilst in the catch-up charge period, the annual catch-up charge will still need to be declared until extinguished.*

Change from cash basis to earnings basis

60. On leaving the cash basis, a barrister may elect for the opening debtors and the work in progress for the subsequent accounting period to be treated as 'adjustment income', the basis of calculation following that discussed at paragraph 57. The 'adjustment income' is brought into charge in equal instalments over six years beginning with the first of the years in which the whole of the adjustment would otherwise be chargeable to tax.

Example:

Lisa commences pupillage in Planet Chambers on 1 April 2018 and elects to join the cash basis, her receipts for the year ending 31 March 2019 being £125,000 with debtors and WIP at the year end of £30,000. In the next year ending 31 March 2020, her receipts are £310,000 and she has to leave the cash basis as the receipts exceed the threshold. At that date her debtors and work in progress (WIP) are £75,000. She elects for the £30,000 to be treated as 'adjustment income'. In the following year ending 31 March 2021, her receipts are £325,000 and her closing debtors and work in progress are £80,000. Lisa's assessable income would be as follows:-

Tax year 2018/19
Cash basis year ending 31 March 2019. £125,000

Tax year 2019/20
Earnings basis for year ending 31 March 2020. £310,000 of receipts plus net movement in debtors/work in progress £45,000, (closing £75,000 less opening £30,000); £355,000, plus Adjustment income 1/6 x £30,000 = £5,000;
Total assessable income £360,000.

Tax year 2020/21
Earnings basis for year ending 31 March 2021. £325,000 of receipts plus net movement in debtors/work in progress £5,000, (closing £80,000 less opening £75,000); £330,000 plus Adjustment income 1/6 x £30,000 = £5,000;
Total assessable income £335,000.

Tax years 2021/22 to 2024/25
Profit on Earnings basis plus Adjustment income to be recognised of £5,000 a year for the four remaining years.

The barrister can make an election to accelerate the charge if desired.

Business records

61. All records necessary to deliver a full and complete tax return must be preserved for five years and nine months following the end of the year of assessment to which

the records relate. Where an enquiry is started into a return, the records must be kept until the enquiry is completed. Copies (including electronic records) are generally acceptable.

Making Tax Digital (MTD) for income tax

62. From 6 April 2024, self-employed barristers with annual business profits and/or property income of more than £10,000 will come within MTD for income tax.

63. Under MTD for income tax, barristers will need to keep digital records. They will also be required to send quarterly summaries of their income and expenditure to HMRC using MTD-compatible software. For barristers on the cash basis, the information to be maintained and compiled for submission will be the professional receipts and payments each quarter. For a barrister on the earnings basis, in principle, adjustments will need to be made for recognition of the quarterly movement in debtors/work in progress/accruals and prepayments. The degree of accuracy expected by HMRC for the quarterly submissions is expected be confirmed closer to the inception date of 6 April 2024. The quarterly submissions would be followed by a final end of year submission to take account of necessary adjustments and a final declaration. This will replace the annual self-assessment tax return.

Reform of basis period rules

64. In preparation for Making Tax Digital, the Government have consulted on reform of the basis period rules, moving from a current year basis to a tax year basis. The headline is that these reforms are due to take effect from 2024/25 but effectively they apply from 2023/24 when the transition takes place. An existing accounting period can be retained but the trading profit for a tax year will become the profit arising in the tax year itself. Broadly this will require apportionment of accounting profits into the tax years in which they arise. Some businesses may decide to change their accounting year end to 31 March or 5 April.

Example:

> *A business prepares accounts to 30 April every year. Currently, income tax calculations for 2024/25 would be wholly based on the profits for the year ended 30 April 2024. The change will mean that the income tax calculations for 2024/25 will be based on 1/12 of the profits for the year ended 30 April 2024 and 11/12 of the profits for the year ended 30 April 2025.*

The change will potentially accelerate when business profits are taxed but a transitional adjustment allows the increased profit to be spread over five years starting

with 2023/24. Any overlap profits brought forward (generally from when the business commenced) will be relieved in full in 2023/24.

At the time of writing, the introduction of a 'Tax Year' basis has already been postponed by one year to the dates mentioned above. Representations are being made to delay it further and to modify it.

Part Two: Advice to Pupils and Barristers Starting Practice

65. This section deals with two questions that barristers and pupils face when they start practice:

a. how should any pupillage award should be treated, and
b. what accounting period should be chosen for their professional profits?

66. These are important decisions, and it might be sensible to seek advice from members of chambers who have recently had to consider these questions themselves, or an accountant knowledgeable in the tax and accounting of practising at the Bar.

Pupillage awards

67. In the past, HMRC accepted that all pupillage awards (whether from the Inns or from the pupil's chambers) have been exempt from income tax in the pupil's hands as "scholarships."

68. HMRC still accepts this as far as awards from the Inns are concerned; nothing in this discussion affects such awards, which are still tax-free. However, since the Bar began formally to encourage the payment of pupillage awards, HMRC has argued that the treatment of chambers' pupillage awards as "scholarships" can no longer be maintained, and that they fall to be taxed as income.

69. Exactly how they should be taxed is, as a matter of strict law, debatable. A case can be made for saying that they are receipts of the pupil's new profession (at least once the pupil has done six months' pupillage and is thus able to accept briefs) and are chargeable as normal professional earnings under Part two of Income Tax (Trading and Other Income) Act 2005 (ITTOIA). Alternatively, it can be argued that they are income chargeable under the general sweep-up provisions.[13]

70. The Bar Council has agreed with HMRC that each pupil may choose in which of the two ways they should be taxed. The options are as follows:

> **Option 1:** The pupillage award in respect of the pupil's first six months will continue to be tax-free, but the award in respect of the second (or subsequent) six months will be included as normal professional earnings in the year of receipt;

[13]See Part 5, Chapter 8 of the Income Tax (Trading and Other Income) Act 2005.

Option 2: Both the "first six" and the "second six" awards will be taxable in the fiscal year of receipt under the general sweep-up provisions.

Matters to be considered in making your decision

71. In cases where the award is modest Option 2 may be preferred. Although the first six award will be charged to tax there may well be little or no tax payable if the barrister has no other income and hence the award is covered, or substantially so, by the tax free personal allowance.

72. In cases of substantial awards, the decision is more difficult. Option 1 will result in the first six award being tax free but there is a potential for the second six award to be taxed, in part, on two separate occasions should the accounting period end early in the tax year. In these circumstances Option 2 is likely to result in less tax being paid but with the liability arising sooner.

73. One other important factor is the liability to Class 4 National Insurance Contributions (NICs). Under Option 1 the pupillage award would be chargeable, but under Option 2 it is exempt. The NIC is, at the time of writing, 9% on profits between £9,569 and £50,270 and 2% on profits above £50,000 so this is an important consideration.

74. It should be noted that under Option 1 no expenses (e.g. travelling) incurred in the first six months would be deductible. Under Option 2 HMRC accept that they would be deductible, subject to the normal tax rules.

Third and subsequent six awards

75. The Bar Council's view is that any awards received in a 'third six pupillage'[14] or any subsequent period, will be treated in the same way as second six awards. That is, if Option 1 is chosen the third six award will form part of fee income and if Option 2 is chosen it will be treated as a separate source of income.

76. It should be noted that HMRC regard the first 12 months pupillage as a period of training and hence there is no liability to Class 2 NICs. Even in the case of third six, or subsequent periods of pupillage, if it can be demonstrated that no substantial fee earning work is carried out, then there is no requirement to make contributions.

Draw down

[14] See paragraph 87 below.

77. In cases where a pupillage award is available for "draw down" before the commencement of the pupillage it is considered that any amounts taken prior to the date of commencement are treated as a loan and not as income until pupillage starts subject, of course, to the terms of the agreement. Most chambers' pupillage agreements provide for any "draw down" to be repaid over the 12 months of pupillage once the student commences pupillage. Thus, by taking a "draw down" tax is not avoided on the amount of the "draw down" as the awards made in respect of the first and second six months 12 months pupillage have to be considered before the deduction of the repayment of the "draw down".

Awards dependent on fees earned or received

78. A further agreement has been reached with HMRC concerning the tax treatment of "first six" and "second six" pupillage awards in cases where the awards are related to the amounts either earned or received during pupillage.

79. HMRC has agreed that a pupillage award which is expressed to be "of an amount equal to the difference between £x and the gross amount received during the period of the award" or alternatively "of an amount equal to the difference between £x and the gross amount earned during the period of the award" will be eligible for the agreed tax treatment described above.

80. It will be apparent that the amount of the award (whether calculated by reference to receipts or to earnings) will be known by the end of the pupillage in question. Insofar as the amount actually advanced by chambers during the pupillage exceeds the award, the excess (repayable out of future receipts) will be regarded as a loan and will be ignored for tax purposes.

General notes

81. The agreement is quite clear that it is the amounts of the pupillage award in respect of the first and second six months that have the choice of treatment. Once the choice has been made, the manner in which the awards are charged to tax then depends on the dates of payment. Generally, a pupillage award should be assumed to accrue evenly over the 12 months unless the Pupillage award agreement states otherwise. For example, if a £30,000 award is assumed to accrue evenly and the first six is treated as tax free £15,000 will be exempt from tax. The £15,000 in respect of the second six will then be taxed in the tax year or years in which it is received. If, however, the agreement states that £20,000 is in respect of the first six and £10,000 is in respect of the second, then £20,000 will be exempt and £10,000 will be taxed in the tax year or years in which it is received.

82. The arrangements outlined above apply to all genuine pupillage awards irrespective of amount and exact date of payment. Payments made by chambers in return for services provided by pupils are not covered by the arrangements but will be taxable in the normal and appropriate manner.

83. In *Edmunds v Lawson*[15] the Court of Appeal held that pupillage is a contract between chambers and pupil for education and training and is not a contract of employment, thus the national minimum wage does not apply and there should be no need to operate Pay As You Earn (PAYE) or employers National Insurance.

84. HMRC accept that a barrister's contribution to pupillage awards made by their chambers is deductible in computing that barrister's taxable profits, whether or not chambers has adopted Trade Protection Association (TPA) status. Additionally, the deduction will not be affected by the tax treatment of the award in the hands of the recipient, as discussed above.

85. The European Working Time Directive[16] applies to pupils at the Employed Bar. It has not been established that it applies to the self-employed Bar but it may be taken as a guide to good practice, at least in relation to holidays.[17]

86. The Department of Work and Pensions (DWP) regarded the whole of the first 12 months of any period of pupillage as a period of training and not of gainful occupation, even though work may be done for a fee under the guidance of the pupil master after the first six months pupillage has been completed. In the decision *Edmonds v Lawson*[18] in the Court of Appeal the Judge commented on the remuneration a pupil receives as follows:

> *[It] cannot be conclusive that pupils are not now generally paid. This is true even of funded pupils since, as we understand, chambers grants are treated as professional earnings for tax purposes only in part. But the fact that the generality of barrister pupils have been unpaid, not just in the distant past but also in modern times, is in our view of significance in determining whether a relationship of or equivalent to apprenticeship exists. For although trade apprentices have always received reduced wages, reflecting both the value of the practical training they receive and their reduced productivity, they have always in modern times received some wages and in earlier times board and lodging… The freedom of a pupil who has obtained a provisional practising certificate to practise*

[15] *Edmunds v Lawson* [2000] QB 501.

[16] See European Working Time Directive 2003/88/EC.

[17] See the Bar Qualification Manual https://www.barstandardsboard.org.uk/training-qualification/bar-qualification-manual-new.html section 4M Support and Advice For Pupils, paragraph 27.).

[18] *Edmonds v Lawson* [2000] QB 501, [2000] 2 WLR 1091.

during the second six months of pupillage, not for the benefit of the chambers or the pupil master but for their own sole benefit and reward, would be highly anomalous if this were anything approaching an orthodox employment or apprentice relationship. While a small point in itself it is in our view another pointer against such a relationship.

87. If a period of pupillage extends beyond 12 months, the DWP had regard to the frequency of paid briefs in deciding whether the extended pupillage constitutes training or gainful occupation. If training is minimal and paid briefs are accepted regularly the DWP regarded the barrister as a self-employed earner.

88. A barrister who has completed their pupillage but cannot find a full tenancy in chambers may become a "squatter" in chambers. The DWP regard a squatter as a self-employed earner.

89. It should be noted that once the "second six" has been completed and the barrister has been issued with a full practising certificate, they are, for all regulatory purposes a practising barrister and the term "third six" has no regulatory meaning. Consequently, a barrister in such circumstances should have their own insurance with the Bar Mutual Indemnity Fund (BMIF) rather than be under the insurance cover of their pupil supervisor.

90. The Bar Council's General Management Committee has taken legal advice and the opinion expressed is that in most cases pupils were unliklely to be "workers" for the purposes of the Pensions Act 2008 and as a consequence did not fall under the auto-enrolment requirements.

Part Three: Starting Practice

91. Barristers who have been in practice and prepared accounts ending before 6 April 2013 rather than prepare accounts on the usual earnings basis are entitled to prepare their accounts on a cash basis for the first seven years of assessment.[19] However this legislation was abolished retrospectively from 6 April 2013 (see paragraph 56) and was replaced with a general cash basis election available to most unincorporated businesses. Barristers preparing accounts on the cash basis under the old legislation (i.e. the old cash basis) are able to continue to take advantage of those provisions and thus can remain in this regime for seven years.

92. The (new) cash basis for Small Businesses was introduced by the Finance Act 2013 and may be adopted by any business subject to certain conditions. To be eligible the business must not be a limited company or a limited liability partnership and the fee income must not be greater than £150,000 for 2021/22. There are a number of other circumstances where a person is ineligible to elect for the cash basis, but these are unlikely to apply to the majority of individuals. Once adopted an individual must leave the cash basis when fee income exceeds twice the VAT threshold (£300,000 for 2021/22).

93. Under the cash basis only expenses actually paid for are allowable as a tax deduction. (The one exception concerns pre-commencement expenditure under the old cash basis where a barrister commencing practice is allowed to claim capital allowances in respect of all expenditure incurred for the purpose of their profession before commencement. In most cases the significance of this will be to allow claims in respect of books bought at university and Bar school, if used in practice, and items such as a wig and gown bought during the first six months of pupillage).

94. Under the cash basis there are some items of expenditure that have special rules:

a. Capital expenditure – provided the expenditure would ordinarily qualify for capital allowances deductions, expenditure on capital items will be deductible as an expense when paid. The only exception being expenditure on motor cars which must be dealt with in accordance with the capital allowances regime. Thus, pre-commencement expenditure is deductible in the first set of accounts prepared for a barrister commencing in practice.

b. Interest paid on loans – if interest is paid on any loan that would ordinarily be deductible this is limited to a maximum deduction of £500.

[19] See section 160 of the Income Tax (Trading and Other Income) Act 2005.

Commencement of practice

95. A number of points should be noted relating to the commencement of practice:

a. Ordinarily, practice will commence on, but not before, completion of the first six months of pupillage. However, if a barrister has a break between first and second six-month pupillages, commencement only at the beginning of the second may be justified;

b. There may be circumstances, however, which justify claiming that practice commences later. For example, if a particular barrister does not hold themselves out as being available for work until after completion of 12 months of pupillage, commencement only after that time may be justified; and

c. Establishing an early date for the start of practice was at one time important because expenditure incurred prior to commencement was not eligible for tax relief. Expenditure incurred in the seven years prior to the commencement of practice is now eligible.

The early years

96. There are particular rules specifying which accounts form the basis of assessment for a particular fiscal year. Generally, the period of account which ends in a particular fiscal year forms the basis of assessment for that year. This means that if accounts are made up to a date early in a year of assessment there is a greater gap between the time money is brought into account and the time tax is due. Moreover, the maximum amount of time will be available to prepare accounts and calculate the tax liability under the self assessment provisions. Generally, the greatest cash flow benefit will be achieved if the first set of accounts is drawn up to a date early in the year of assessment following that in which practice commenced. Subsequent sets of accounts will use the same date. 30 April may be regarded as a convenient terminal date.

97. The law is found in Chapter 15 of Income Tax (Trading and Other Income) Act 2005 (ITTOIA). The effect is as follows:

98. **First year:** The basis period for the first tax year of practice:

a. begins with the date on which one commences in practice, and
b. ends on the following 5 April.

99. **Second year:** The basis period for the second tax year of practice is:

a. the twelve-month period of account ending in the tax year following the year of commencement, or

b. if there is no twelve-month period of account ending in the tax year following of commencement more complicated rules, apportioning the profits of one or more accounting periods, are brought to bear.

Example 1

Lisa commenced on 20 April 2020 and prepared her first accounts to 30 April 2021, showing a profit of £36,000. Accounts are subsequently prepared to 30 April each year. She would be taxed as follows:

- *For 2020/21, the proportion is 351 days (from 20/4/2020 to 5/4/2021) divided by 376 days (from 20/4/2020 to 30/4/2021), so the assessable profits are £33,606.*

- *For 2021/22, the proportion is 365 days (from 1/5/2020 to 30/4/2021) divided by 376 days, so the profits are £34,946, and*

- *For 2022/23, she will be taxed on her accounts for the year ended 30 April 2022; for 2023/24, the profit to 30 April 2023 et seq.*

Example 2

Daniel's first period of account covered three fiscal years so the profits would be divided between those years in the same way. So if Daniel commenced on 31 March 2020 and made up his first accounts to 30 April 2021, again showing a profit of £36,000, his taxable profits in the years concerned would be:

- *For 2019/20, the proportion is six days (from 31/3/2020 to 5/4/2020) divided by 396 days (from 31/3/2019 to 30/4/2020), so assessable profits are £545.*

- *For 2020/21, the proportion is 365 days (from 6/4/2020 to 5/4/2021) divided by 396 days, so profits are £33,181, and*

- *For 2021/22, the proportion is again 365 days (this time from 1/5/2020 to 30/4/2021), so profits are again £33,181.*

Example 3

Mark commenced on 6 April 2020 and prepared his first accounts to 5 April 2021, showing a profit of £36,000. Accounts are subsequently prepared to 5 April each year. He would be taxed as follows:

- *For 2020/21, the profit to 5 April 2021,*
- *For 2021/22, the profit to 5 April 2022, et seq.*

Example 4

Elizabeth commenced on 1 May 2020 and prepared her first accounts to 31 December 2020 showing a profit of £24,000. Accounts are prepared to 31 December in following years, those to 31 December 2021 showed a profit of £40,000. She would be taxed as follows:

- *For 2020/21, the proportion is the full first period, 245 days, (from 1/5/20 to 31/12/20) plus 95 days (from 1/1/21 to 5/4/21). So assessable profits are £24,000 + £10,410 (£40,000 x 95/365). A total of £34,410.*
- *For 2021/22, the year ended 31 December 2021 £40,000, and*
- *For 2022/23, the profit to 31 December 2022, et seq.*

100. As can be seen, the first set of accounts a barrister draws up may affect the liability to income tax for one or two (or even three) years of assessment. The principle underlying the current rules, however, is that the profits of a practice will be assessed only once over the life of that practice. Where the same profits, or part of the same profits, form the basis for more than one year of assessment, the overlap profits are determined, and these may be set off on either a change in accounting date which involves a period of account of more than 12 months, or the cessation of practice.

101. The earlier the date in the fiscal year to which accounts are made up, the greater the deferral and the greater the overlap period is. For example, comparing two barristers who earn approximately the same amounts after commencement:

Example 1

Richard starts practice on 1 May 2020. He makes up his first set of accounts to 5 April 2021 and they show a profit of £36,000. He makes up his second set of accounts to 5 April 2022 and they show a profit of £45,000. He would be taxed as follows:

2020/21	*£36,000*
2021/22	*£45,000*

2022/23	*Profits to 5 April 2023 (likely to be more than £45,000).*

No overlap profits occur so no overlap relief will be available for future use.

Example 2

Jessica also starts to practise on 1 May 2020. She makes up her first set of accounts to 30 April 2021 and they show a profit of £36,000. She makes up her second set of accounts to 30 April 2022 and they show a profit of £45,000. She would be taxed as follows:

2020/21	*£33,534 (340/365 of £36,000)*
2021/22	*£36,000*
2022/23	*£45,000*

Jessica's overlap profits are those for the period 1 May 2020 to 5 April 2021, that is, £33,534.

Clearly Jessica, by sole virtue of her accounting date, is paying less tax than Richard in the early years.

102. In different circumstances, different accounting periods may be appropriate. Before drawing up your first set of accounts all considerations relevant to your particular circumstances should be addressed. This is a most important decision, and it may well be sensible to seek advice from members of chambers who have recently had to consider these questions themselves, or an accountant knowledgeable in the accounting and tax issues of practising at the Bar.

Timetable

103. Under self assessment, tax for each year of assessment is paid by way of two instalments on account: 31 January in the year of assessment and 31 July after the end of the year of assessment. The payment on account is generally 50% of the previous year's liability, unless there is reason to believe that the following year's liability will be smaller. Any additional tax is due on 31 January following, once the actual liability has been ascertained. In respect of the year of commencement, however, no payments on account will have been made, so all the tax for the year will be due on 31 January following the end of the fiscal year in which practice commenced. At that time, the first payment on account for the following year will also be due. In total, an amount of 150% of the tax due in respect of the profits for the first year of assessment must be paid.

Notification dates

104. For a barrister starting pupillage in September 2021, commencing in practice on, say 10 April 2022, and with no other income, the important dates are as follows.

105. If choosing to tax the entire pupillage award as miscellaneous income:

a. notify HMRC immediately on commencement of practice, if HMRC have not been notified by 5 October 2021 a penalty may be levied
b. file first return by 31 October 2022 (if filing a paper return), and
c. pay tax by 31 January 2023 (and file return if filing by internet).

106. If choosing the first six award tax-free route:

a. notify HMRC immediately on commencement of practice, if HMRC have not been notified by 5 October 2022 a penalty may be levied
b. file first return by 31 October 2023 (if filing a paper return), and
c. pay tax by 31 January 2024 (and file return if filing by internet).

This example assumes there are no other sources of income or gains that have their own return filing requirements.

National Insurance contributions

107. All self-employed individuals must register with HMRC in order to make National Insurance Contribution (NIC). There are two classes of contributions relevant to the self employed: Class 2 and 4.

Class 2 contributions

108. These contributions are a flat rate of £3.15 per week for 2022/23. These contributions are collected with income tax for the year as set out above.

109. A penalty is charged if there is a failure to notify liability to Class 2 NICs before 31 January following the end of the fiscal year in which the Class 2 contributions should have been paid.

Class 4 contributions

110. These contributions are calculated on the profits chargeable to income tax for a given fiscal year at 10.25% of profits between £11,908 and £50,270 and then 3.25% on profits over £50,270. The contributions are paid with the income tax for the year as set out above.

Notification

111. By completing a form CWF1 http://www.hmrc.gov.uk/forms/cwf1.pdf and sending this to HMRC this will ensure that both the notification requirements for Income Tax and NIC have been complied with. This form should therefore be submitted well before the dates set out above.

112. Alternatively, and perhaps more conveniently, it is possible to register on line this can be completed by going to this URL: https://www.gov.uk/log-in-file-self-assessment-tax-return/register-if-youre-self-employed

Part Four: Capital Allowances and Chambers Expenditure

113. If you buy an asset (e.g., a computer, a table) for use in your practice you cannot deduct the cost of that asset from your profits, unless you are applying the cash basis of accounting applicable from the tax year 2013/14 onwards. Instead, you may be able to claim a capital allowance for that expenditure. The relevant statutory provisions are contained in Capital Allowances Act 2001 supplemented and amended by later Finance Acts. HMRC guidance can be found on their website.

114. For those on the cash basis (see Part 1) expenditure on assets used for business purposes is generally an allowable deduction when paid, as though it were a revenue expense. However, to be so allowable the asset must be such that it would be eligible for capital allowances under the earnings basis. This general rule does not necessarily apply to cars (see below).

Expenditure and allowances

115. Expenditure incurred on "plant and machinery" used for business purposes is eligible for capital allowances. To qualify, the expenditure must be of a capital nature and the barrister must own or be capable of becoming the owner of the asset (e.g., hire purchase) as a result of incurring the expenditure.

116. There are three allowances relevant to barristers: the Annual Investment Allowance (AIA), the First Year Allowance (FYA) and the Writing Down Allowance (WDA). Broadly, the AIA provides for 100% relief against income on qualifying expenditure in the year of purchase, subject to monetary limits. The FYA provides for a 100% relief in the year of spend on certain categories of new plant and machinery. Writing Down Allowances are annual allowances which are claimed on the balance of capital expenditure on qualifying plant and machinery ineligible for either the AIA or the FYA or otherwise where these allowances are not claimed. Please note that the 130% Super-deduction applying to expenditure incurred during the two-years ended 31 March 2023, will generally not apply to barristers as it is applicable to companies only. It will apply to incorporated Chambers or Chambers established as Trade Protection Associations (see Part Five), but further advice is outside the scope of this summary.

Annual Investment Allowance

117. The AIA provides 100% relief, subject to monetary limits. These limits have changed frequently. From 1 January 2016 to 31 December 2018 the first £200,000 of qualifying expenditure was eligible. The limit was increased to £1m from 1 January

2019 to 31 December 2020, and is set to reduce from 1 January 2023 to £200,000 again. Cars are excluded from the AIA.

118. The AIA is claimed for the accounting period in which the expenditure is incurred. The AIA is proportionally increased or reduced where the accounting period is more or less than a year. It is time-apportioned where the accounting period overlaps a change in the maximum allowed. The AIA cannot be claimed in the final period of account ending with the death or retirement of a barrister.

119. Where an accounting period straddles a change in the limit the rules for calculating the maximum AIA are complicated.[20] It may be of relevance to Chambers registered as a TPA or as a chambers service company.

120. In general, the AIA will provide a 100% allowance for qualifying expenditure incurred by a barrister leaving the WDA available to relieve any balance of expenditure not covered by the allowance (e.g., incurred before the AIA was introduced)

First Year Allowance

121. Expenditure on certain limited types of asset and for certain limited periods is eligible for enhanced allowances known as First Year Allowance.

122. A 100% FYA was available on designated energy-saving and/or environmentally beneficial plant and machinery up to 5th April 2020. A 100% FYA is also available on certain low carbon-dioxide-emission cars, initially provided the expenditure was before 1st April 2021, but extended to 1st April 2025. (11 March 2020 HMRC announcement on HMRC website).

Writing Down Allowance

123. A WDA is currently available on the reducing balance basis at 18% of the balance of any expenditure not covered by the AIA and any balance of expenditure brought forward from previous years. It is not available on expenditure for the year of acquisition where FYA is claimed. Certain special rate expenditure qualifies at only 6%. The main type of such expenditure is integral features of buildings, such as electrical installations or thermal insulation. (See paragraph 128 below)

124. The WDA is claimed for an accounting period. It is proportionally increased or reduced where the accounting period is more or less than a year. It is time-

[20] For detailed guidance please refer to HMRC (http://www.hmrc.gov.uk/manuals/camanual/ca23085.htm).

apportioned where the accounting period overlaps a change in the rate of allowance (As an example for the year ended 30 June 2012 the WDA rate is 19.53% following the change in rates from 20% to 18% on 6 April 2012.)

125. Where the written down value of a plant and machinery pool is not more than £1,000 a WDA equal to the entire value of the pool can be claimed.

Example

> *Josephine buys a desk for her room in chambers for £1,600, in July 2020 and makes up her accounts annually to 30 June. She previously incurred expenditure and the written down value brought forward at 1 July 2019 was £950. The example assumes AIA will continue for future years and shows how its effect for typical levels of capital expenditure is to leave no balancing amount subject to the more restrictive 18%. Her expenditure will qualify for the following capital allowances which she may set off against her profits for the corresponding years:*

		Allowances
Accounts to 30 June 2020		
Balance brought forward	*950*	
Write off pool	*(950)*	*950*
Accounts to 30 June 2021		
Balance brought forward	*0*	
WDA @ 18%	*(0)*	*0*
Cost of desk *AIA@100%* *Accounts to 30 June 2022*	*1,600* *(1,600)*	*1,600*
Balance brought forward	*0*	
WDA @18%	*0*	*0*

126. In general, all qualifying expenditure is aggregated, known as "pooled" for capital allowance purposes with the consequence that it is unnecessary to make separate calculations for each item of plant and machinery. After deducting the allowances, the resulting balance is known as the "main pool." Expenditure on various types of assets is excluded from the main pool including assets used partly for business purposes, integral features of premises and certain cars.

Private use

127. Relevant expenditure incurred on an asset used partly for business use must be included in a separate single pool. Allowances are calculated in the normal way and then the amount claimed for tax purposes is restricted for private use on a just and reasonable basis.

Integral features and special rate

128. Expenditure on integral features of premises for which a WDA is given is included in a special pool. The rate of WDA for such features is currently only 6%. Integral features include electrical (including lighting systems), cold water, heating and ventilation systems and lifts. As the WDA applies after deduction of the 100% AIA this special pool will not normally apply to individual barristers, given that the AIA is £1m until 31st December 2022, and £200,000 thereafter., but it may apply to expenditure by chambers. However, the favourable position is dependent upon the AIA limit. Reductions to it have frequently occurred in the past, the limit being as low as £25,000 in 2012.

129. Where the cost of repair on an integral feature is more than 50% of the cost of replacing the entire integral feature, it is required to be treated as a capital replacement (again generally likely to be relevant for chambers only).

130. Expenditure on equipment at a private residence which is used wholly or partly for business purposes may also qualify for capital allowances.

131. Until a profession or trade ceases, balancing allowances or charges may not occur, and individual items of plant can continue to attract WDAs at an ever-decreasing rate long after the item has been sold or scrapped. However, where expenditure is on assets with a short life, particularly computer equipment, they can by irrevocable election form their own separate pool of expenditure. Provided the expenditure is expected to be written off over a shorter period of less than eight years the election may be advantageous. However, the ability to claim AIA of up to £1,000,000 (from 1st January 2023 £200,000) and write off pools with less than £1,000 means that this facility is more appropriate to chambers' expenditure than to individual barristers.

Leasing

132. Relevant expenditure incurred using hire purchase or using leasing where the leasing agreement provides that the barrister shall or may become the owner, is eligible for capital allowances purposes.

133. Where the agreement does not provide for ownership to pass to the lessee, but the asset is "capitalised" in the accounts in accordance with accounting standards, the

lessee can claim the finance interest and depreciation charged in the accounts on that asset as a deduction for tax purposes.[21] This is not relevant to barristers applying the cash basis who claim relief for expenditure on a paid basis.

134. Otherwise, where assets are rented rather than purchased, the rental payments may be deducted in full for tax purposes since they are regarded as revenue payments (with the exception of motor vehicle leasing). Accordingly, the respective merits of purchasing or leasing assets should therefore be considered in the light of the differing tax treatments.

Motor vehicle leasing

135. For leases of cars commencing before April 2009 a formula was applied to establish the proportion that may be deducted which would then itself be reduced for any personal element.

136. Currently for car leases (other than for electric or low emission vehicles) there is generally a disallowance of 15% of the hire cost. This will apply where the car in question has carbon dioxide emissions of more than 50g per kilometre, this figure applying to expenditure incurred from 6th April 2021 (reduced from 110g).

Motor Cars

137. Generally, allowances are based on carbon dioxide emissions. Electric cars and those with carbon dioxide emissions of not more than 0g per kilometre acquired new after 5 April 2021 (reduced from 50g) qualify for a 100% allowance. This means business cars acquired after then with emissions up to 50g will no longer qualify for FYA, but will be eligible for WDA at the main rate of 18% if exclusively used for business). For emissions in excess of 50g the expenditure is allocated to the 6% special pool (along with, for example, integral features as discussed above) or in its own 6% pool where private use is relevant which in most cases it will be). For expenditure incurred between 6 April 2018 and 5 April 2021 substitute 110g for 50g. From 6 April 2013 to 5 April 2018 substitute 130g. Prior to 6 April 2013 use 160g.

138. In almost every case, there will be a degree of non-business use of a vehicle so that the corresponding proportion of the allowance is disallowed. This is regardless of when the car was acquired, and each car used privately needs to be kept in a single asset pool.

139. As mentioned in the section on motoring expenses, HMRC look to taxpayers to keep records of business and private mileage in order to justify the proportion claimed

[21] See HMRC Statement of Practice 3/91.

as business use. They will often ask for such records as part of self-assessment enquiries.

140. On the sale of a motor vehicle that has been used for business purposes, the sale proceeds are compared with the written down value and, subject to adjustment for non-business use, the resulting excess or deficit is charged or allowed in the profit computation of the barrister for the year of the disposal. These are referred to as balancing charges and balancing allowances, respectively and are calculated independently from other capital allowances.

141. For barristers on the cash basis, capital expenditure on cars can be calculated using the capital allowances rules. Alternatively, the mileage rate (see Part 1) can be used to cover both capital and running costs in which case there will be no claim for capital allowances.

Pre-commencement expenditure and/or change of use

142. A barrister commencing in practice is allowed to claim capital allowances in respect of expenditure incurred prior to commencement. The expenditure is treated as if it had been incurred on the first day of practice. In most cases, the significance of this rule is that claims are allowed in respect of earlier purchases of books and computer equipment and items such as a wig and gown.

143. A barrister may introduce into the practice an asset originally acquired for a non-business purpose (e.g., a car) where the qualifying expenditure is taken as the lower of cost or market value at the date it is brought into use.

Discontinuation of practice

144. On ceasing to practice, the disposal proceeds of assets sold together with the market values of assets retained are compared with the tax pool of unallowed expenditure. In the same manner as that described above for motor vehicles, this will result in balancing allowances if the unallowed expenditure is greater than the disposal proceeds or in balancing charges if the disposal proceeds are greater than the unallowed expenditure.

Leaving and entering the cash basis

145. Where a barrister who joins the cash basis from the earnings basis, has any balances in the capital allowances tax pools (except in relation to cars), this may be claimed as an allowable deduction in the first accounts under the cash basis provided it has been fully paid for. Where the asset is used partly for private purposes, the deduction should be restricted accordingly.

146. On leaving the cash basis to enter the earnings basis, any unrelieved qualifying expenditure, e.g., such as under a hire purchase scheme, can be allocated to a new capital allowances pool in the subsequent accounting period.

Capital Allowances and Computation of Profits

147. There are a number of situations in which the accounts computation of profits departs from the computation of profits for tax purposes. Commercial accounts must provide for loss of value (value consumed) each year in relation to capital assets employed in the business. Depreciation is a mechanism for writing off the cost of fixed assets over their predicted useful economic life. Depreciation records a reduction in the value of fixed assets arising from their use in the business. Fixed assets for these purposes would include computers and furniture. In the commercial accounts these will be depreciated each year, and depreciation will appear as expenditure in HMRC accounts. For tax purposes, depreciation is non-deductible and has to be added back to profits. Instead, traders can claim capital allowances, which can then be deducted from profits for tax purposes.

Example

Nick has an accounting period ending on 30 April. On 1 May 2021 the tax Written Down Value (WDV) of his existing computer was £1,533. On 1 March 2022 he buys a laptop for use in his practice for £1,000. His commercial accounts show profits of £60,000, after deducting depreciation of £280.

His capital allowances are (for accounting period ended 30 April 2022):

Item		*Capital allowances*	*Values c/f*
Opening value (computer)	*1,533*		
WDA @ 18%	*(276)*	*276*	
Closing value			*1,257*
Additions (laptop)	*1,000*		
AIA @ 100%	*(1,000)*	*1,000*	
Closing value			*0*
Total		*1,276*	*1,257*

His accounts for tax purposes will show:

Profits per accounts	*60,000*
Add back deprecation	*280*

Total	*60,280*
Less: capital allowances	*(1,276)*
Taxable profits	*59,004*

Part Five: Chambers Expenses, TPAs and Service Companies

148. This part examines the tax treatment of chambers' contributions and alternative structures for chambers

Chambers expenditure

149. Whilst it may seem obvious that contributions to chambers expenses should be fully tax deductible as business expenses in the accounts of the individual barrister, the matter is not always that straightforward.

150. At its simplest, a set of barristers' chambers can be seen as a cost sharing vehicle where a group of individuals have banded together to share common business expenses. An unincorporated set of chambers is not a separate entity as a matter of general law or for direct tax purposes and therefore the tax treatment of members' contributions will depend on when and how those monies are applied by chambers. That is to say, it is not the contributions that members pay into chambers that determines the tax deduction in their accounts, but rather how chambers has used those contributions.

151. Where some items of chambers expenditure do not qualify for a tax deduction, or are of a capital nature, the members should adjust their own accounts to reflect this.

152. Chambers must advise each member of their share of any non-tax deductible expenditure. This information must include the date on which the costs were incurred to allow the members to make the appropriate adjustments to their accounts.

153. Chambers must also advise each member of their share of any chambers capital expenditure that qualifies for capital allowances. Again, this information must include the date on which the capital expenditure was incurred. Further, where a chambers has surplus funds because members' contributions have exceeded chambers' expenditure, this should also be reflected in members' accounts. Members' contributions must have been expended by chambers for them to be tax deductible, and so chambers must advise each member of their share of unexpended chambers contributions.

154. The apportionment of these adjustments can be administratively complex where members have different accounting year ends, and where some members prepare their accounts on the cash basis, whereas others use the earnings basis. Chambers records need to be kept in a manner that permits them to identify the tax adjustments so that the relevant information can be provided to the members.

155. Barristers need this information if they are to complete their self assessment tax returns correctly. It is open to HMRC to enquire into a barrister's tax return to ensure that the correct tax treatment has been applied. If on enquiry it is found that chambers has not provided this information to a member, there is a likelihood that this could trigger enquiries into the tax returns of all the members of that set.

156. Simply incorporating chambers, by setting up a service company, does not circumvent the tax difficulties. Members' contributions to these service companies are treated as mutual income, and the "mutual trading" rules apply. Consequently, the service company is transparent for tax purposes, and the tax deductibility of members' contributions to such companies depends on the end use of those contributions, in the same manner as if chambers was unincorporated and the company did not exist.

157. Chambers organise themselves in widely differing ways, and the purpose of what is written here is to alert barristers to the problem, rather than to provide solutions for every situation. The apportionment of expenses is dealt with differently in different sets of chambers. Whatever system is used, it is important that it aims to charge for a year only the amount actually expended by chambers in the year.

Treatment of chambers as a Trade Protection Association

158. The situation is much simplified if chambers adopt the arrangements applicable to Trade Protection Associations (TPAs).

159. The main practical effect of the TPA arrangement is that chambers is deemed to be a taxable entity in its own right. It is assessable to corporation tax and any tax adjustments are made in chambers' tax computation. The members of chambers can treat their chambers contributions as being fully tax deductible for the purposes of their own accounts and they do not have to concern themselves with how chambers has used those chambers contributions.

160. Chambers wishing to adopt TPA status should write to HMRC at Corporation Tax Services, HM Revenue and Customs, BX9 1AX. The letter should enclose:

- A copy of the chambers constitution
- A copy of the latest chambers accounts
- A list of the members of chambers

161. HMRC should then write to say that the TPA arrangement has been approved in principle, sending three copies of a document setting out the terms of the agreement. All three copies require signature (by the Head of Chambers and Chambers' Treasurer) and will need to be returned to HMRC. One copy will be signed on behalf of HMRC and returned to chambers.

The tax consequences for chambers

162. As a TPA, chambers must prepare accounts in accordance with Generally Accepted Accountancy Practice. Profits arising from members' contributions would be computed using the rules for income from a trade. Losses, caused by a deficiency of members' contributions, would be computed using the same principles as used to calculate profits, and may be carried back and relieved against profits of the previous six years or profits of future years.

163. Contribution rebates may be deducted in arriving at the profit for tax purposes.

164. The charge to tax would be at the applicable corporation tax rate (currently less than marginal income tax rates) and normally payable nine months and one day after the end of the accounting period.

The tax consequences for the barrister

165. An individual barrister's chambers contributions to the TPA are wholly deductible in their own accounts whether on a cash or earnings basis. There is therefore no requirement for the barrister to obtain details of how and when their contributions have been applied by chambers.

The VAT consequences for chambers

166. TPA status has no effect the VAT position of chambers or of its members. TPA arrangements are only relevant to direct taxes: corporation tax and income tax.

Service companies

167. Simply setting up a service company does not circumvent the tax difficulties associated with a set of chambers which has not adopted TPA status[22]. Contributions to these service companies are treated as mutual income, and the "mutual trading" rules apply. Consequently, the service company remains transparent for direct tax purposes, and the tax deductibility of members' contributions to such companies depends on the end use of those contributions, in exactly the same manner as if the company did not exist. It is, however, open to service companies to apply for TPA status in the same way as chambers generally. The same procedures would need to be followed as described above.

[22] Typically, a service company is set up as a non-profit making company limited by guarantee with the members of chambers becoming members of the company.

168. Some chambers have formed service companies to assist in the general administration of chambers. Such companies may have commercial advantages (e.g., limited liability). Fiscal considerations applicable to such companies are complex and are not covered in this guidance. It is considered that there are no real fiscal advantages in adopting service companies. A set of chambers proposing to form a service company to own chambers' assets should seek particular tax advice of its own.

169. There are additional costs involved with running a service company. The accounts must comply with Companies Act requirements and accounts have to be submitted to Companies House and a corporation tax return must be submitted to HMRC.

Specialist Bar Associations

170. There are numerous Specialist Bar Associations that barristers become members of and to which they pay regular subscriptions. The subscriptions paid will normally be tax deductible in the accounts of the paying barrister. However, as with a set of chambers if the association uses the subscriptions for settling expenditure that would not be tax deductible if paid by the barrister then strictly a proportion of the subscription would not be tax deductible in the barrister's accounts. A similar problem arises if the association makes a profit out of the subscriptions and retains that surplus.

171. In addition, if the association puts on events that are open to non-members for a fee and makes a profit from the event there is a corporation tax liability on that part of the profit that relates to non-members.

172. These difficulties can be dealt with in a simplified manner if the association registers with HMRC as a TPA. The Specialist Bar Association will have to pay corporation tax on all profits, but the subscriptions of the members will be fully tax deductible without any concerns over the use to which those subscriptions have been put.

Part Six: VAT and The Bar

173. Value Added Tax (VAT) is a tax levied on the supply of goods and services by a person registrable for VAT. In general, VAT will apply to a barrister's fees.

174. The relevant statutory provisions are contained in the Value Added Tax Act 1994 (VATA) supplemented and amended by later Finance Acts and Statutory Instruments. HMRC have issued a VAT guide (VAT Notice 700) which is of general application.

175. The VAT Notice 700 may be considered valuable as a background to the information provided here, which is designed to be of specific use in explaining how the tax applies to barristers, and how barristers and their clerks should deal with the necessary documentation.

What must be paid

176. In principle VAT is a tax to which barristers are chargeable on the services they render in the exercise of their profession. In general, the services provided are either taxable supplies or outside the scope supplies. Taxable supplies are subject to VAT at the rate of 20% currently. Outside the scope supplies attract no UK VAT charge. Accordingly, once registered a barrister must account for VAT on all taxable supplies made in the course or furtherance of their profession. Taxable supplies extend, for example, to a sale by the barrister of any of their chamber's furniture and, unless a separate employment is involved, to fees for lecturing and writing articles. The barrister must charge VAT on such supplies and account for it to HMRC. Furthermore, the accounting for VAT will include any other business activity the barrister undertakes in their own individual capacity that may be entirely unrelated to their work as a barrister. Registration, and the requirement to register, applies to the individual person in respect of all business supplies the barrister makes, not just those made in the course of their professional chambers work.

177. In general VAT is not payable by barristers until fees for their services are actually received (provided the fee note is not a tax invoice: see below). The actual receipt of fees by barristers will almost invariably include VAT and the moment of such receipt is called the tax point. This moment will fall in a tax period, each of such periods being of three calendar months, for which a VAT return is required to be made to HMRC.

178. The standard rate of VAT has been 20% since 4th January 2011. Typically, this means that barristers will levy 20% to their base (ex VAT) fee charged for professional work as the total receipt is regarded as including VAT. This 20% is called output tax.

179. Consideration for goods and services is inclusive of VAT unless otherwise stated (e.g., if a barrister agrees to a fee of £600 for lecturing, £100 is VAT unless the agreement makes it clear that the fee is exclusive of VAT). This is an essential principle to bear in mind when agreeing a fee for any services provided. The barrister must guard against the risk that they have to account to HMRC for VAT out of a fee which they had assumed was exclusive of VAT. Fees should be quoted as (for example, "£1,000 plus VAT" (if that is the intention) not just "£1,000".

180. Subject to the deductions mentioned below, VAT must be accounted for and paid by barristers to HMRC by one month and seven days after the end of the tax period in which the particular fee is received. If the deadline falls on a weekend or a bank holiday the payment must be received by the last working day beforehand. All VAT registered businesses have to file VAT Returns. This must be done within the same one month and seven-day period following the VAT period as for VAT payments.

181. Thus, a barrister who charges £1,000 plus VAT for a piece of work must account for an additional £200 representing output tax. If they receive that total sum of £1,200 on 1 November and the next VAT period ends on 30 November, they must pay the £200 VAT element to HMRC by 7 January, together with all other VAT received between 1 September and 30 November, but subject to the deduction for all input tax in the course of their profession during that period.

182. "Input tax" is the name given to VAT charged by a supplier on goods or services used by the barrister in the course or furtherance of their profession (i.e., VAT which has been paid by the barrister).

183. Devilling fees paid to a barrister who is registered for VAT are liable to VAT which should therefore be added to the fees and included in the recipient's quarterly return. The payer takes credit for the VAT as deductible input tax in their quarterly return and is entitled to be given a tax invoice for it. The result is neutral in the sense that the VAT cost to the barrister and the devil is nil, but it is important that barristers and their devils should know the strict legal position.

184. If a barrister, in carrying on their practice, uses certain services supplied from outside the UK, then they are deemed to have supplied those services in the UK. Accordingly, they will have to account for VAT on the value of the supply received from abroad, but unless the circumstances are unusual, they will also be entitled to a corresponding input tax credit, so there is no net effect. This process is called "the Reverse Charge." It is a mystifying mechanism at first sight, but it may help to understand it by reference to the apparent policy reason for its existence, which is to

prevent distortion of competition by removing any VAT advantage in a UK business outsourcing services it needs from the UK to non-UK suppliers.

Part-time Judicial appointments and other offices

185. As indicated above, once a barrister is registered, VAT will apply to all supplies made in the course or furtherance of their profession. Section 94(4) of VATA provides that:

> *Where a person, in the course or furtherance of a trade, profession or vocation, accepts any office, services supplied by him as the holder of that office are treated as supplied in the course or furtherance of the trade, profession or vocation.*

186. As a matter of law, therefore, it might well be that remuneration of a barrister holding a part-time judicial appointment could be subject to VAT. Any appointment to an office needs to be considered from this aspect. As stated below, not all appointments are regarded as being taken in the course or furtherance of the profession.

187. HMRC treat certain such appointments as outside the scope of VAT. The HMRC *Business/Non-Business VAT Manual* (Reference VBNB41400 - Specific issues: judicial appointments)[23] states:

> *Judicial appointments*
>
> *Full time, salaried judicial appointments, although technically public offices, are not covered by section 94(4). This is because the services are regarded as supplied in the course of employment.*
>
> *Part-time judicial appointees who carry out the same functions and have the same powers as their full-time colleagues are not treated as making supplies in the course or furtherance of business*

188. Examples of part-time judicial appointments outside the scope of the tax given by HMRC are:

- Deputy High Court Judge
- Recorder
- Deputy Circuit Judge/Assistant Recorder
- Deputy Metropolitan Magistrate
- Deputy Provincial Stipendiary Magistrate

[23] https://www.gov.uk/hmrc-internal-manuals/vat-business-non-business/vbnb41400

- Deputy County Court and District Registrar
- Deputy Master/Registrar of the Supreme Court or High Court
- Deputy Assistant Chancery Registrar
- Coroner
- Deputy and Assistant Coroner
- Dean of the Court of Arches
- Auditor of the Province of York (Church of England)
- Assistant Local Government Boundary Commissioner
- Temporary Supreme Court Judge (Scotland)
- Temporary Sheriff Principal (Scotland) and
- Temporary Sheriff (Scotland)

189. It is considered that in practice this treatment may extend to part-time judges and members of the Tax Tribunal and other Tribunals. However, in view of the absence of an express statement to that effect in HMRC manuals, any barrister in this position should take specific advice, and, as appropriate, obtain a ruling from HMRC.

190. Section 94(4) of VATA only applies in terms to "offices." Accordingly, it is important to note that where a barrister is employed to carry out some particular function and is taxed under PAYE as employment income rather than as professional income, VAT will not be chargeable, as section 94(4) would not as such apply. For example, a barrister may be retained to give a series of lectures either on a self employed basis as part of their profession or in a separate employment capacity. Only in the first case would they have to account for VAT.

VAT paid on receipts

191. VAT on supplies made by barristers is chargeable at the earliest of the following times:[24]

a. when the fee is received
b. when the barrister issues a VAT invoice, or
c. the day when the barrister ceases to practice.

192. Accordingly, if a practising barrister wishes to postpone the tax point to the time of payment, they should ensure that their Fee Note is not a VAT invoice[25], as otherwise the VAT element will then arise and become due for payment one month and seven days from the end of the quarter involved, even though the fees are still outstanding.

[24] See VAT (General) Regulations 1995, S.I. 2518, Regulation 92. This rule does not apply to "Entities" (see chapter 10) for whom the standard time of supply rules apply – see section 6 VAT 1994. They may be eligible to use cash accounting discussed further in this chapter.
[25] See Reg. 92.

This possibility of postponement also applies to part payments when a VAT invoice should only be issued for the amount received, but not the amount outstanding (for which a further fee note could be issued at the same time as the invoice).

193. The position on retirement or death is set out in Part Seven (paragraphs 376 to 377). Subject to that, if the procedure set out in paragraph 258 below on "Tax Invoices" is adopted, the tax point will always be the day when the fee is received.

194. VAT is not due on any interest charged on fees paid late.

Legal aid Crown Court defence work, fee sharing protocol

195. As discussed at paragraph 49, under the Advocates Graduated Fee Scheme (AGFS), the Legal Aid Agency pay the entire advocacy fee for the case to the "Instructed Advocate" who is the advocate who undertook the trial. Out of that fee, the advocate is responsible for paying any other advocates who covered hearings in that case ("Substitute Advocates"). The Bar Council have produced a Graduated Fee Payment Protocol[26] which sets out how the fee should be divided. Most chambers have software for doing this calculation automatically.

Fees payable to the Instructed Advocate

196. The total fee for the case will be paid to the Instructed Advocate together with VAT (if they are VAT registered). Where it is necessary for a Substitute Advocate to undertake any advocacy services that will be as subcontractor.

197. The Instructed Advocate will be liable to account to HMRC for the VAT on the value of the whole supply made. The Substitute Advocate (if VAT registered) will be required to invoice the Instructed Advocate and account for VAT on the value of the supplies made to the Instructed Advocate. The Instructed Advocate may, however, reclaim (on their VAT return) the VAT which was made accountable to them by a Substitute Advocate, on these supplies as input tax, subject to normal VAT rules.

198. Appropriate records must be kept for VAT inspection, including copies of VAT invoices issued by the Instructed Advocate and VAT invoices issued to the Instructed Advocate by any Substitute Advocate. The Bar Council recommends that chambers keep these records centrally.

Registration threshold

[26] https://www.barcouncilethics.co.uk/documents/graduated-fee-payment-protocol/

199. This is dealt with in more detail in the sections below. In essence a barrister is liable to be registered if the value of their annual supplies (from practice and any other business supplies) exceeds £85,000 or there are reasonable grounds to believe that it will exceed such a figure within the next thirty days taken from any point of time. Persons whose annual turnover does not reach these figures may apply for voluntary registration.

Deductible sums – Input Tax

200. Before paying over to HMRC the VAT element in their receipts, the barrister is entitled to deduct any VAT added to the cost of the goods or services for which they have paid and has received a tax invoice in the course of their practice during the same tax period. They may, for instance, have bought stationery for £100 in that period, carrying an additional VAT element of £20 and incurred hotel bills of £200 carrying an additional VAT element of £40. They are entitled to set off against their VAT liability for that tax period the sum of £60 which they have paid out as VAT charged by others. This sum of £60 is called input tax and is deductible against their output tax. For income tax purposes £300 of the above mentioned expenses may be treated as deductible expenditure against their income tax liability, but the £60 is not so deductible since it reduces their VAT liability and is wholly recovered. A different option is available under the cash basis of accounting where receipts and expenses may include VAT – see paragraph 39e, with the quarterly VAT payments treated as an allowable expense when paid or conversely, as a taxable receipt when refunded by HMRC.

201. Where a barrister does not claim input tax on supplies against the output tax on their supplies, for example because they are below the registration limit and not voluntarily registered, the total cost of their purchases, including the VAT element, may be deducted for income tax purposes. In practice the principle of deducting for income tax what is not recovered for VAT purposes may extend more widely, (e.g. if input tax relief is denied because of lack of an appropriate VAT invoice) but as this course would only give the barrister relief in respect of the input tax at their highest rate of income tax, it is always preferable to recover the VAT element in full and they should endeavour to retain all VAT invoices in respect of their inputs and recover the input tax against the output tax.

The expenses which attract and do not attract VAT

202. Input tax incurred can only be reclaimed where it is incurred for business purposes and must not be specifically disallowed by statute (e.g., entertaining, and private motor cars). Furthermore, some expenditure is exempt, zero-rated, or outside the scope of VAT, that is does not involve incurring VAT in the first place. A barrister

cannot recover any input tax on expenditure in these latter three categories, as none will have been paid.

Standard rate expenditure attracting the tax

203. Examples of expenses that are standard-rated for VAT are:

a. Computer costs.
b. Stationery.
c. Repairs and renewals.
d. Accountancy charges.
e. Telephone, including mobile charges.
f. Off street parking.
g. Hotel bills.
h. Subsistence when away from chambers.
i. Car repairs and servicing.
j. Car, petrol and oil.
k. Subscriptions to law libraries, as distinct from purchase of law books.
l. Taxi fares (if the driver is registered for VAT).
m. Devilling charges (if the devil is registered for VAT).
n. Robes, wigs, collars, bands, two dark suits and six tunic shirts for appearance in Court.
o. Robing room fees for locker use.
p. Chambers' contributions - where a VAT invoice is issued.
q. Capital expenditure (e.g., furniture, equipment but not books or sets of cases).
r. Domestic fuel and power (e.g., electricity and gas) attracts VAT at a lower rate, currently 5%.

204. In all these instances it is assumed that the supplier is registered for VAT. If they are not registered, they cannot add VAT to their fees so there is nothing to reclaim. The barrister should always obtain a VAT invoice in respect of any of these supplies, otherwise the VAT may not be deductible.

205. As indicated above a barrister can deduct for VAT purposes the input tax on the cost of a dark suit and similar items of clothing purchased specifically for Court wear: *Alexander v. Customs and Excise Commissioners*.[27] HMRC are prepared to accept limited claims where the dark clothing would not have been purchased but for Court requirements. The effect of this decision is confined to VAT. The VAT rules are less stringent than the "wholly and exclusively" test for income tax, discussed elsewhere in this guidance. Consequently, this input tax may be deducted even though the

[27] See *Alexander v. Customs and Excise Commissioners* [1976] VATTR 107.

barrister is not entitled to deduct the actual cost of such clothes for income tax purposes.

206. Examples of expenditure which is exempt from VAT include:

a. Insurance premiums.
b. Bank charges.
c. Rent of chambers and other accommodation for professional purposes (unless the landlord has exercised their option to charge VAT at the standard rate).
d. Bar Council, Circuit, Specialist Bar Association and other professional Association subscriptions.

207. Examples of zero rated expenditure include:

a. Books and other publications including from 1 May2020 certain e-books.
b. Newspapers / Magazines.
c. Travel by public transport.

208. Examples of expenditure outside the scope of the tax altogether include:

a. Wages and National Insurance of the barrister's employees.
b. Council Tax.
c. Payments for services or goods from non-registered persons.
d. Parking fines.

VAT and chambers expenditure

209. VAT registered barristers are entitled to deduct from their VAT payments all input tax in relation to the VAT elements of their chambers expenses. Thus, for example, the cost of a new computer paid for by chambers as a whole will carry a VAT element which can be deducted by the registered barristers in those chambers in whatever proportion is appropriate.

210. Different chambers adopt different systems for charging and apportioning chambers expenditure. There are three general systems which HMRC are prepared to accept. The three systems are set out below.

211. There is no requirement that sets adopting the Trade Protection Association (TPA) arrangement for income tax must be registered separately for VAT purposes. The TPA arrangement is simply a contract between a set of chambers and HMRC and does not in itself affect the VAT position. Many sets adopting the TPA arrangements

have applied to be registered for VAT, but this is not necessary and whether it is advisable will depend on the circumstances of the set and its members.

212. Other sets have arranged for the incorporation of a service company. It is usual for the service company to register for VAT in its own right so that the following provisions will not apply.

Method 1 - Supplies by the Head of Chambers or other nominated member

213. The nominated member, to whom the invoice has been addressed, treats the full amount of VAT as input tax. Output tax is accounted for on the shares charged to all the other members of chambers.

214. Those members who are VAT registered are entitled to deduct the VAT charged to them as their input tax.

215. As a concession by HMRC, tax invoices need not be issued by the nominated member. However, to help HMRC to ensure that no more than the total VAT stated on the invoice is deducted, it will be necessary for each member's records to be cross-referenced to:

a. output tax charged by the nominated member,
b. the input tax deducted by other members, and
c. the original tax invoice.

216. The records of all members of chambers must be available during a VAT control visit by HMRC to any one of them.

Method 2 - Proportional attribution of input tax

217. The nominated member, to whom the invoice has been addressed, does not charge output tax on the members' contributions. The input tax on the supply is apportioned so that VAT registered members may deduct it on the basis of their own contributions.

218. Records must be kept of the apportionment of input tax between the members of chambers. Each member's records should cross-reference the input tax deducted to the tax invoice.

219. The records of all members of chambers must be available during a VAT control visit by HMRC to any one of them.

Method 3 -The combination method

220. The nominated member, to whom the invoice has been addressed, deducts the whole amount of input tax but also pays an equal amount into the common fund. This method may only be used when all members of chambers are registered for VAT.

221. Special accounting rules apply to those barristers or advocates who are on the flat-rate scheme and whose chambers use Method 3.

222. Sets of chambers are free to adopt whichever of the above methods best satisfies their needs. Once a particular system has been adopted it is recommended that the system be maintained. The concern of HMRC is of tax claims by all the members of chambers exceeding the actual input tax suffered on supplies to chambers. Consequently, adequate records of the manner of attribution etc. should be maintained so that the position can readily be checked by HMRC.

223. Alternatively, the chambers itself may be registered for VAT as described below.

Chambers registered for VAT

224. If a set of chambers or a chambers service company is registered for VAT, it will have to account for VAT on the supplies it makes to members of chambers and will receive credit for input tax paid on the supplies it receives. Whether the chambers have to levy VAT on all supplies to members will depend on the precise circumstances. For example, if the set makes separate supplies of accommodation (paid for by rent) and general administrative services (paid for by a percentage contribution), the percentage element will attract VAT but the rental element will be liable for VAT if and only if the set has exercised the "option to tax" in respect of its premises. The set should issue invoices to members who will then, if themselves registered for VAT, be able to reclaim the VAT element.

225. This system may be administratively simpler than those outlined above but results in a cost for those members who are not themselves registered and could lead to the earlier payment of VAT by members. Care should be taken in choosing the chambers VAT quarters relative to those of members. Before registering for VAT, a set of chambers should seek appropriate professional advice.

VAT and personal expenditure

226. VAT registered barristers may also deduct the VAT element in their business expenditure paid personally against their output tax.

Example

Fiona is a London based barrister who does a two-day case in Birmingham. Her expenses may look like this:

Item	*Expenses*	*VAT*
Taxi to Euston	*15.00*	*3.00*
Taxi to hotel	*12.00*	*0.00*[28]
Hotel bill	*100.00*	*20.00*
Lunches	*20.00*	*4.00*
Train fares	*115.00*	*0.00*
Taxi Euston to chambers	*15.00*	*3.00*
	£277.00	*£30.00*

The sum of £30.00 can be deducted in the relevant quarterly return against output tax, whether or not the fees for that case were paid in the same period. The sum of £277 should qualify for deduction against income tax as ordinary professional expenses, but the sum of £30.00 does not, on the basis that it has been claimed in the VAT return as input tax.

Obligatory registration

227. A barrister is required to be registered:

a. if the value of their taxable supplies (whether as a barrister or otherwise) in the previous 12 calendar months has exceeded £85,000. The barrister must advise HMRC within 30 days, with registration applying from the end of the month following that in which the barrister exceeded the limit. Or

b. at any time if there are reasonable grounds for believing that the value of their taxable supplies within the next thirty days will exceed £85,000[29] (with registration applying from the start of the thirty-day period).

228. If the fees of a barrister (inclusive of the monetary amount of any other taxable supplies they may make from other activities) who is not registered exceed the figure of £85,000 for any year they are still not obliged to be registered if HMRC can be satisfied that the value of their total taxable supplies in the following year will not exceed £83,000.

229. The figures of £85,000 and £83,000 referred to above have been applicable since 1 April 2017 and may be increased by subsequent Treasury Orders.

[28] Taxi driver is not VAT registered.

[29] See VAT Act 1994, Schedule 1, paragraph 1, as amended.

Voluntary registration

230. Even though a barrister may not be obliged to register under the tests set out above they may apply to be registered voluntarily. This is a personal decision for the barrister concerned. Reasons why a barrister with a tenancy might wish to register voluntarily include:

a. A barrister who registers can claim recovery of their input tax against their VAT liability. Otherwise, this is not recoverable, and the barrister will only be able to obtain relief against their income tax liability.

b. Their clerk can commence a system of accounting which can be permanently adhered to without alteration, and which is identical to that of the other members of their chambers.

c. They do not disclose to their clients that their gross earnings are comparatively low.

d. Their chambers can only use the third method of dealing with VAT on chambers expenditure described above if *all* members of chambers are registered.

e. In Crown Court defence Advocates Graduated Fee Scheme work, it will avoid the financial disadvantage of, as an Instructed Advocate having to pay to a Substitute Advocate a sum inclusive of VAT, but being unable to claim from the Legal Aid Agency the fee inclusive of VAT (see paragraphs 195 to 198).

231. It might be thought that barristers in the early stages of their career would be at a disadvantage in voluntarily registering for VAT as they would be obliged to account for VAT when other, unregistered barristers in a similar position are not charging VAT. However, this is not invariably so and depends upon the source of work undertaken. In particular instructing solicitors can generally claim back as their own input tax the VAT so charged, and the VAT the solicitors themselves must charge may be to commercial or business clients who can recover the VAT themselves.

232. There will, however, be a relative disadvantage where fees are borne by clients who cannot reclaim the VAT element themselves, that is where private client work predominates.

What follows registration

233. The form by which the barrister applies for registration is VAT1.[30] Shortly after a barrister's application has been accepted and they are registered they will receive from HMRC a certificate of registration (VAT 4), stating their registration number. This number must be used in all subsequent communications with HMRC and must appear on all VAT invoices of registered barristers which are tax invoices. The barrister will also be told the effective date of their registration, that is to say the date from which their obligation to charge output tax and their entitlement to deduct input tax will start. A registered barrister is also under an obligation to notify HMRC of any change of professional address and of their retirement.

234. The quarterly return period will also be advised. The barrister can apply for this to be altered to a more conventional date (e.g., to coincide with their annual accounting date).

Deregistration

235. A barrister ceases to be liable to be registered at any time, if they can satisfy HMRC that the value of their taxable supplies in the period of one year then beginning will not exceed £83,000 (this figure is applicable from 1 April 2017 but can be changed by Treasury Order).

236. The current Form for deregistration is VAT 7. [31]

Retirement or death

237. The provisions for deregistration set out above apply where the barrister continues to carry on their practice but the value of their supplies has fallen. Ordinarily it would not be recommended that they should seek to deregister in such circumstances.

238. Where a barrister retires which includes discontinuance for any other reason (e.g., to take up full-time employment) they should notify HMRC of the fact within thirty days, using form VAT7. HMRC will then cancel their registration.

239. When a barrister dies whilst in practice, their clerk should inform HMRC as soon as possible of the death. The personal representatives of a deceased barrister should likewise inform HMRC within 10 days of the grant of probate or letters of administration whether they wish to elect for the deferment procedure.

[30] https://www.gov.uk/government/collections/vat-forms
[31] https://www.gov.uk/government/collections/vat-forms

240. References should be made to Part Seven of this guidance regarding discontinuance generally. Technically[32], the output VAT on all of the barrister's work completed prior to the date of retirement or death becomes payable. However, HMRC are prepared to allow[8] payment of the VAT as and when the fees are received, provided the barrister or their personal representatives make a specific election (referred to as "deferment") shortly after the cessation of practice. It is considered that such an election will almost invariably be advisable. It has been agreed with HMRC that, when they receive an application for deregistration by or on behalf of a retired or deceased barrister, they will send in reply a copy of their leaflet explaining the special arrangement for post-cessation receipts of barristers and the appropriate form for election to defer payment of VAT until the fees are received. That form must be completed and returned to the HMRC if VAT is not to be paid at once on all outstanding fees.

241. Where deferment of the liability has been accepted by HMRC in these circumstances, a form will be sent to the barrister or their representative, on which is to be listed:

a. all the outstanding fees subject to the standard rate of VAT,
b. the name of the relevant case,
c. the professional client, and
d. the date of the first fee note.

242. Subsequently HMRC will send each quarter a form which will be used to show:

a. any fees which have been received in the period,
b. any fees for which a VAT invoice has been issued in the period, or
c. any fees, previously shown as free of VAT, which are now subject to the standard rate.

243. After the first year, the barrister may choose to submit the form on a six monthly basis, until such time as all the fees have been collected. At this stage the declaration on it "declaration of final payment" may be completed. This finalises the matter. In the event there are fees outstanding which the barrister or personal representative determines cannot be collected, the reason should be stated in the declaration of final payment.[9]

244. On deregistration the barrister is deemed to have supplied (at market value) all goods then owned which had been acquired for the purposes of their profession and

[32] See VAT (General) Regulations 1995, Regulation 92.
[8] See *VAT Notice 700/44/20 Barristers and Advocates; VAT Notice 700/11/18 Cancelling Your* Registration

on which they had claimed an input tax deduction, and account for output tax thereon. This usually applies to capital items. Subsequent actual sales of the goods will not attract VAT.

245. Any input tax incurred after registration has been cancelled may be repaid by HMRC on submission of a separate claim using Form VAT 427. The claim must normally be made within six months of deregistration, but in any case within four years of the date on which the input tax arises.

The need to maintain records

246. Every taxable barrister must keep records of all services they supplied and the goods and services they received in the course of their profession in sufficient detail, for a minimum of six years[33]:

a. to allow them to calculate correctly the amount of VAT they have to pay HMRC,
b. to allow them to calculate the amount of money they can offset against their VAT liability,
c. to complete the necessary VAT returns, and
d. to provide documentation to allow HMRC to check the completeness and accuracy of these returns.

247. In particular they must retain VAT invoices in respect of supplies so as to enable them to recover the VAT thereon as input tax.

Making Tax Digital For VAT

248. From April 2019 mandatory changes were made to the VAT record-keeping requirements, which essentially requires VAT-registered barristers to keep most of their financial records digitally and to prepare and file their VAT Returns using HMRC accredited software. These record-keeping requirements are known as Making Tax Digital for VAT (MTDfV). Initially, the requirements applied to barristers who had a turnover above the registration threshold of £85,000. From April 2022 they apply to virtually all VAT-registered barristers, with very limited exception.

249. HMRC has published VAT Notice 700/22: Making Tax Digital for VAT, which sets out the requirements in detail.

250. Under MTDfV, VAT registered barristers are required to keep most of their financial records digitally. It thus goes beyond the record keeping rules in VAT Notice

[33] See para 2.4 *Notice 700/21/16* "Record keeping."

700/21. Coupled with this, VAT returns must be calculated and submitted to HMRC electronically using MTDfV compatible software via what is known as an Application Programming Interface (API).

251. The VAT return can be submitted from accounting software, bridging software or API-enabled spreadsheets. The fundamental point is that transfer of data to HMRC, from the mandatory digital records to the filing of the return, must be entirely digital.

252. As manual VAT record keeping is not acceptable, the records have to be kept digitally, using 'functional compatible software'. This means a 'software program or set of compatible software programs which can connect to HMRC systems via an API', which must be capable of:

- Keeping records in digital form as specified by the rules.
- Preserving digital records in digital form for up to six years.
- Creating a VAT return from the digital records held in compatible software and submitting this data to HMRC digitally.
- Providing HMRC with VAT data on a voluntary basis.
- Receiving information from HMRC via the API platform.

253. Records to be kept digitally are specified in the VAT Notice 700/22 at paragraph 3.3.17. For these, the software must record the different rates of VAT applicable to each supply (where more than one rate applies on an invoice). For supplies received, the amount of input tax claimed on each invoice will need to be shown.

254. MTDfV is not completely paper-free, and it does not mean businesses are required to provide digital invoices, or to only accept digital receipts. Some records may still be kept in hard copy if the barrister chooses to do so, e.g., purchase receipts, although these can also be scanned and kept electronically. It is the actual recording of supplies made and received that must be digital. Where invoices and receipts are not kept electronically, they must be kept in hard copy as usual for VAT purposes.

255. The VAT return is still a nine-box return. But under MTDfV, it is completed by your software pulling in data from the digital records.

256. The digital records required for MTD do not have to be held in one place or one program. Thus, a barrister like any business may keep digital records in a range of different compatible digital formats, just so long as the format chosen is MTDfV compliant. For example, one barrister may choose to maintain their records using accredited commercial accounting software; whereas, another barrister may prefer to use spreadsheets in combination with add-on MTD software. Regardless of the digital form the records may take, it is a mandatory requirement that the information forming

part of what HMRC calls the 'digital journey' – the mandatory submission process – is transferred via 'digital links'.

257. Section seven of the VAT Notice outlines acceptable digital links, including:

- Linked cells in spreadsheets.
- Emailing a spreadsheet with digital records to an agent, for the agent to import data into software to make a calculation, such as a partial exemption calculation.
- Transferring digital records onto portable devices and giving these to an agent.
- XML, CSV import and export, download and upload of files.
- Automated data transfer.
- API transfer.

258. For barrister's fees, it is recommended that barristers liaise with the Chambers administrator in ascertaining how their fees information will be provided to them (e.g. as a CSV file or spreadsheet), since the desire here will be for it to be provided in a digital format capable of being read by the barrister's own accounting records, thus complying with the digital links requirements. Chambers administrators should consider contacting their diary system provider in considering this further.

259. HMRC does not provide MTDfV software. Rather it maintains a list of accredited software packages on its website. Barristers should be aware that a number of the software packages listed on HMRC's website for MTD store data in the "cloud". If VAT data is stored on servers outside the UK, that will result in a transfer of data outside the UK. The data that is required to be kept in the compatible software does not have to have any client personal data included, because fee notes / invoices can be cross referenced to the actual document stored on the Chambers fee system. If, however, the data transferred onto the compatible software includes invoices addressed to an individual client including details of the work undertaken for them, such personal data cannot be transferred outside the EEA unless certain conditions have been met. In such circumstances, barristers should establish where any proposed software provider stores data in order to ensure that the relevant data protection rules are not breached. The Bar Council IT Panel's guide to Cloud Computing is available on the Bar Council's Ethics and Practice Hub[34].

260. Exemption from MTDfV is broadly limited to those satisfying HMRC that, for reasons of age, disability, remoteness of location or for any other reason, it is not reasonably practicable for them to use digital tools to keep business records or submit

[34] https://www.barcouncilethics.co.uk/documents/cloud-computing/

returns. It is likely that the exemption will apply in only the most limited of circumstances.

Tax invoices

261. Except where a barrister ceases practice, the tax point is the earlier of the issue of a tax invoice and payment. So as to ensure that the VAT only becomes due when the fee is paid, barristers may wish to ensure that fee notes which their clerks issue prior to the receipt of any fees do not constitute tax invoices. This can be achieved by ensuring that the fee notes so rendered do not bear a distinct VAT invoice number and contain a box, left blank, for the insertion of the date on which the fee is subsequently received, which will constitute the tax point. Once the fee is paid a tax invoice should be sent to the solicitor, or other instructing professional, bearing a distinct invoice number and having inserted upon it the date on which the fee was received and which is, therefore, the tax point.

262. A VAT invoice should contain the following information:

a. A unique, sequential tax invoice number.
b. The date of the tax point (generally payment).
c. The barrister's name, address, and VAT registration number.
d. The professional instructor's name and address.
e. Details of the work done.
f. The nature of the services charged for (which will always be professional services).
g. The amount of the fees charged for each item.
h. The total fees (i.e. the taxable amount).
i. The rate and amount of VAT charged.

263. Fee notes rendered prior to payment do not need to be formal VAT invoices and, therefore, should not contain these requirements where the barrister has chosen to defer the tax point until payment.

Local Authority payments[35]

[35] This section deals with VAT when working for local authorities. With regards to income tax when working for local authorities, the following extract from the Bar Council's "Remuneration related Ethics and Practice FAQs" https://www.barcouncilethics.co.uk/documents/remuneration-related-ethics-and-practice-faqs/ may be of interest:
"Q.27.) I am a self-employed barrister who sometimes does work for a local authority. The local authority has sent me an IR35 letter. I am concerned that the effect could be that I would no longer be self-employed for tax purposes. What should I do?
ans.) The "IR35" rules apply where an entity contracts with a personal service company ("PSC") for the services of an individual in circumstances such that, in substance, the individual is an employee of

264. The Bar Council has been asked to provide practical guidance on the issue of formal invoices for local authority work and the related VAT implications. The background to this request is that, whilst VAT on services generally becomes due at the earliest of (a) provision of the service (b) payment and (c) issuing of an invoice, there is a special rule for barristers, whereby VAT on supplies made by barristers is chargeable at the earliest of the following times: a) when the fee for the barrister's service is actually received (b) when the barrister issues a VAT invoice, or (c) the day when the barrister ceases to practice. Whichever of these dates applies to any set of circumstances is called the "tax point". The "tax point" for a barrister is normally the receipt of the fee. This follows the practice whereby a fee note/request for payment is issued initially, followed later by a formal VAT invoice on receipt of the fee.

265. However, the Bar Council is aware that an increasing number of local authorities have now changed their payment practices, so that they will only pay on advance receipt of the formal VAT invoice. Where this occurs, it follows from 2b) above that the "tax point" becomes the date of issue of the VAT invoice. A number of enquiries have been received expressing concern that such an arrangement potentially exposes the barrister to having to fund the VAT out of their own resources. This is because the VAT may become due for payment to HMRC before payment is received from the local authority.

266. In response, the Bar Council recommends that barristers consider adoption of HMRC's scheme "Cash Accounting Scheme for VAT". Subject to eligibility, this is a facility generally available to businesses provided that their annual fee income is expected to be less than £1.35m (including disbursements but excluding VAT and capital items). Under the rules of the Scheme, VAT is accounted for to HMRC each quarter on the basis of payments received and made (rather than by reference to the tax point of supplies made and received). In practical terms, this means that regardless of when a VAT invoice is issued by the barrister, the VAT will only become due to HMRC for the quarter in which payment is received. In so doing, the concern of the barrister having to fund the VAT prior to settlement of the invoice is removed.

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that entity (or would be but for the insertion of the PSC). If the rules apply, amounts received by the PSC are treated as the earnings of the individual and the PSC is liable to operate PAYE etc. What changed on 6th April 2017 is that, where public sector entities contract with PSCs, it is the public sector entity not the PSC which now has to assess whether or not the rules apply and if the rules do apply operate PAYE etc.

This is all very unlikely to be relevant to barristers. First, few barristers will use PSCs. Secondly, of those few, very few will enter into arrangements amounting to quasi-employment. It may be possible for, say, someone specialising in care cases to work mainly for a single local authority and possibly in such a way that he or she was a quasi-employee – but it is unlikely that such a person would use a PSC.

In light of this, barristers receiving letters like this can ask for the assessment to be carried out as soon as possible so that they can continue to be paid as self-employed contractors in the usual way."

267. The Scheme does have the drawback of only enabling VAT on expenditure to be reclaimed on a payments (as opposed to on an invoice) basis. For the vast majority of barristers, this is unlikely to be of any real significance, but barristers should review their own circumstances in deciding whether to adopt "cash accounting" for themselves. The use of the VAT cash accounting scheme does not affect the billing practice for non-local authority work which would continue to be transacted in the normal way of issuing the VAT invoice on receipt of the fee. The Scheme can be joined at the start of a VAT quarter or at the outset of VAT registration, subject to the estimated income for the next twelve months ahead being less than £1.35m. After joining, a barrister can remain in the Scheme until annual turnover exceeds £1.6m. There is no need for a barrister to inform HMRC of the decision to join or leave the Scheme, although their own records should be noted accordingly. See paragraphs 332-342 below for further details of the Cash Accounting Scheme. For detailed guidance, barristers should follow the following link to HMRC's website: http://www.hmrc.gov.uk/vat/start/schemes/cash.htm#top, and/or consult with their tax advisors.

Changes in rates of VAT

268. In the case of barristers' fees, the rate of tax payable will often be the rate in force at the time at which the fees are received by the barrister. However, if the rate of VAT goes up, the position may be different. It may be that barristers' fees paid after the change are subject to liability at the old rate if the fees relate to services rendered before the change of rate.[36] Whenever there is a rate change there is also usually anti-forestalling legislation which also needs to be considered.

269. There was a change to the VAT rate from 17.5% to 20% on 4th January 2011. Detailed guidance on this change, as it affects barristers was issued at the time and is reproduced as Annex 1. It should also be noted that those on the flat-rate scheme are affected differently than those not on the scheme. The principles involved are likely to apply to future VAT rate changes.

VAT on fees outstanding at registration

270. Most barristers do not become registered for VAT before they receive their first sets of instructions, and therefore they will probably have undertaken a number of items of work before their registration takes effect. This will apply to many pupils in the second six months of their pupillage.

[36] See VAT Act 1994, Section 88 (2), and VAT (General) Regulations 1995/2518, Regulations 92 and 95.

271. If a fee note is issued in respect of such work before the barrister is registered the fee note will not show any VAT as an addition to the fee. If the fee is paid before the barrister is registered there is no difficulty, but a problem arises if payment is received after the barrister has become registered, for work carried out beforehand.

272. It would obviously be inconvenient for barristers if VAT had to be accounted for after registration for work performed before registration, and the Bar Council regards the legal position as not entirely clear. HMRCs view is that VAT should be levied on all fees received after the date of registration[37].

273. However, HMRC accept that the point is not wholly free from doubt and, since only small sums of VAT are usually involved which in practice would probably either be deductible as input tax by the instructing solicitor or would fall on legal aid funds, they are normally prepared to accept that VAT need not be accounted for on fees received by barristers in such circumstances.

274. Therefore, when a barrister becomes registered it should be unnecessary for their clerk to send out new VAT inclusive fee notes in substitution for those still outstanding at the time. However, HMRC have been concerned in the past that solicitors should not misunderstand the position and deduct tax which barristers have not accounted for. The arrangement is therefore subject to the condition that fee notes issued in such circumstances should specify the date the work was performed and have stamped or written on them, the following words:

> *Note: This is not a VATable invoice. No VAT is included in this fee.*

275. Since this is a possibly concessionary practice of HMRC, in an earlier edition of this Handbook the following text from the then relevant Customs and Excise Manual[38] was reproduced in full:

> *5.1 Fees outstanding at registration*
>
> *In nearly all cases most barristers will have fees outstanding due to them at registration for work undertaken prior to VAT registration. If a receipted fee note is sent out before VAT registration, no VAT should be shown for the work undertaken.*

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[37] See Regulation 92 of the VAT (General) Regulations 1995 [S,I.1995/2518] (services shall be treated as taking place at whichever is the earliest of the fee being received or an invoice issued).

[38] HMRCs V1-37 – Control Notes - Section 5 Accounting information are no longer extant having been archived, and the text not reproduced elsewhere, but the practice is considered to be normally still followed.

However, from the VAT registration date fees will be paid for work undertaken prior to registration. ***A newly registered barrister is not required to account for VAT on fees that were outstanding at the time of registration.*** *(Our emphasis)*

In these cases barristers or their administrative clerks should ensure that no VAT is shown on the receipted fee note and it is quite clear that the recipient should not claim any input tax in relation to the fee. The actual tax invoice should show the actual date the work was performed, and to avoid any misunderstandings the phrase "This is not a VATable invoice" should be clearly printed on the receipted fee note issued.

If part of the work is undertaken prior to registration and part after but a request for payment [occurs after registration] sent out and payment is made, VAT should be charged on the total cost of the service provided, ***unless the actual dates and work performed are shown on the fee note.*** *(Our emphasis)*

276. Where registration and requests for payments take place prior to the issue of receipted fee notes, even though some of the relevant work may have been performed prior to registration, the view of HMRC is that VAT must be accounted for. This creates no practical inconvenience for the barrister, and the Bar Council recommends that in such cases the fee note should add VAT to the basic amount of the fee in the usual way.

VAT and insured clients

277. The usual practice in issuing fee notes applies to work undertaken for insurance companies. This remains the case even if the insurance company acts through an in-house solicitor. A barrister cannot properly issue a fee note/invoice net of VAT to the insurance company and a separate note/invoice for the VAT to the lay client (the insured) in the hope that the lay client can recover the VAT even though the insurer (who cannot normally recover VAT) has paid the fee.

278. Under rC30.9c of the Bar Standards Board Handbook, the Cab Rank Rule applies to instructions received under "the Standard Contractual Terms for the Supply of Legal Services by Barristers to Authorised Persons 2020." Under those Terms, the barrister looks for payment from the solicitor, not from the lay client.[39]

279. Strictly speaking, the fee should not be regarded as comprising a fee element plus a separate VAT; rather the fee is a single amount inclusive of VAT (even if described as, say, "£1000 plus VAT"). This customary treatment is recognised in the concession permitted by HMRC whereby the fee note is issued to the solicitor and the

[39] https://www.barcouncilethics.co.uk/documents/contractual-terms/

solicitor, after obtaining the approval of the barrister, may re-address it to the lay client for the latter to pay direct to the barrister.

280. It may be that the insurer in these circumstances has an arrangement with the client whereby the client pays the insurer an amount equal to the VAT on the barrister's fee, or even pays the barrister an amount equal to the VAT, because the client can recover it, but the barrister should issue a single fee note in the usual way, after which the barrister issues a VAT invoice for the fee to the insurer for the full amount. The insurer can pass this on to the client, so the result is the same as if separate fee notes had been issued.

281. It is understood that the special concessionary procedure whereby it is possible to treat the supply of a barrister's services as having been made directly to a solicitor's overseas client does not apply in the case of insurance companies and their customers. The barrister should issue a single fee note in the usual way, after which they should issue a VAT invoice for the fee to the insurer for the full amount.

Special concessionary procedure in relation to legal services with a foreign element

282. *De Voil* states at V6.135

> *HMRC seem to take the view that a barrister is regarded as making supplies of legal services to the instructing solicitor (or other person entitled to instruct him). Accordingly it will be the place where the solicitor has their business rather than the location of the solicitor's client that will determine where any legal services provided by the barrister are supplied.*

283. Nevertheless, a concessionary procedure was agreed between HMRC, the Law Society and the Bar Council for a barrister's fees paid into and kept in a solicitor's client account. It was adopted when VAT was first introduced and the procedure was published in the 4 April 1973 edition of Law Society Gazette. *The Law Society's VAT Guide* also refers to it. It should be noted that the concession only applies to solicitors, despite the fact that other professionals are now authorised to instruct barristers.

284. Under this procedure it is possible for the instructing solicitor to treat the supply of a barrister's services as having been made directly to the ultimate client. This entails the solicitor re-addressing the barrister's fee note by inserting the client's name and address and the word "per" immediately before the solicitor's own name and address or crossing out the solicitor's own name and address and replacing it with the client's name and address. Once receipted, the fee note should be passed by the solicitor to their client thus enabling them to treat the VAT as input tax, if they are a taxable person and the supply of barrister's services was obtained for the purposes of their business.

285. If, because of the nature of barrister's services and the identity and location of the solicitor's client, the supply of those services is not subject to UK VAT, for example legal advice to a business abroad, the solicitor is entitled to certify the fee note accordingly and ask their client to pay the VAT exclusive amount only. Alternatively, they may ask the barrister's clerk to cancel the original fee note and submit a new one; this will have no adverse VAT implications in that the barrister's fee note only becomes a tax invoice when receipted. In either case, the fee note will have to be addressed to the ultimate client.

286. It is important to note that it is the UK solicitor who decides whether to adopt the concessionary treatment. It is not the barrister; if the solicitor does not elect for the concessionary treatment, VAT remains chargeable under the general rule.

287. As stated previously this concession does not apply to insurance companies and their clients.

VAT and work for foreign clients

288. In view of the concession referred to above which UK based instructing solicitors may elect to use to treat a barrister's legal services as generally supplied to the ultimate client, it is relevant that there are rules which apply that treat legal advice as outside the scope of UK VAT when supplied to a person who belongs abroad. They may also be directly applicable to barristers, should instructions be accepted from outside the UK instead of from a UK solicitor.

Client "belonging" overseas

289. When the client "belongs" overseas, the supply will invariably be outside the scope of VAT, being deemed to have been made outside the UK. The one notable exception is for legal services relating to UK land – see paragraph 293 below.

290. The supply will be outside the scope, firstly, if the client "belongs" in a country outside the UK (other than the Isle of Man). Under this heading it is not relevant whether the supplies are for private or business purposes. It is sufficient that the client is outside the UK.

"Belonging"

291. The country in which a person "belongs" can be a complex matter and advice should be taken for any case which is not straightforward such as where the client appears to be based in several countries or has branches or places of business in the UK.

292. If the case in question is legally aided, you should also consider the Legal Aid Agency's guidance on this issue.[40]

Exclusion of land services

293. Legal services related to UK land are always supplied in the UK and chargeable to VAT. Conversely legal services related to land outside the UK are outside the scope of UK VAT, being deemed supplied where the land is located.

294. HMRC state that legal services such as conveyancing or dealing with applications for planning permission are covered by this rule; whereas services with no direct land element, such as the legal administration of a deceased person's estate which happens to include property, are not so covered and remain general legal services.

Car expenses

"Business Use" and "Private Use"

295. As noted in paragraph 202 input tax incurred can only be reclaimed where it is incurred for business purposes and must not be specifically disallowed by statute (e.g. entertaining and private motor cars).

Fuel

296. Provided a barrister uses their car at least partly for "business" purposes, they have an option of claiming all the VAT they pay on all fuel purchases as input tax, subject to obtaining and retaining supporting invoices in the usual way.

297. However, assuming that they use the car at least partly for private use, which will almost invariably be the case, they must account for "output tax" at a flat rate according to a scale which depends upon the car's CO_2 emissions. The scale charge is the same whatever the private mileage in the VAT quarter.

298. The only alternatives to adopting the scale charge are; for input tax to be apportioned on a mileage basis between business and non-business/private use, and thus the use of detailed time-consuming logs of every journey; or, alternatively, for no input tax to be claimed at all on road fuel.

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[40] See Section 4 of the Legal Aid Agency's *Costs Assessment Guidance* for civil work completed under the relevant LAA civil contract https://www.gov.uk/guidance/funding-and-costs-assessment-for-civil-and-crime-matters

299. The quarterly "output tax" scale charge applicable from 1 May 2022 increases in steps starting with £29 for cars with CO_2 emissions of 120 g/km (or less) to £102 for emissions over 225 g/km. These charges usually change annually on 1 May, and when there is a change in the VAT rate.

300. Assuming the scale charge is adopted, the barrister should include the amount of VAT due under the appropriate scale in Box 1 of their VAT Return.

301. Barristers should consider carefully whether they travel sufficient "business" miles to justify claiming VAT on petrol. It may be advisable to opt out of accounting for VAT using the scale charges by not reclaiming input tax on any fuel bought, whether they use it for business or private motoring.

Leasing or Hiring a Vehicle

302. When a barrister leases or hires a vehicle at least partly for "business use", they may reclaim 50% of the VAT incurred on the rental.

Repairs and Maintenance

303. Provided that the barrister uses their car at least partly for "business use", they may treat *all* the VAT paid on repairs and maintenance as input tax. This applies even if the car is used partly for private purposes.[41] If a car is hired with a contract that incorporates servicing and repairs, the leasing company may be able to apportion the VAT to show that which is attributable to the leasing charges (VAT deduction restricted to 50%) and that attributable to servicing etc. (VAT fully deductible).

Purchase of a car

304. A barrister cannot reclaim *any* VAT on the purchase or importation of a car, unless it is used wholly for business use and is only available for such business use. A car is available for private use when there is nothing preventing private use. Therefore, generally input VAT cannot be claimed on the purchase of a car.

305. "Purchase" means not only outright purchase but also any purchase made under a hire-purchase, lease-purchase or other agreement whereby property in the car eventually passes to the purchaser.

VAT returns

[41] VAT Notice 700/64/14 para 5.1

The barrister's personal records

306. For the purposes of recording their personal expenses, which are relevant to both VAT and income tax, a barrister may find it convenient to keep a VAT and expenses book in which can be entered all of their professional expenses. HMRC are entitled to demand to see receipts (tax invoices) for any items on which it is claimed that input tax is deductible. Such documents should be retained for six years after the end of each accounting period.

The quarterly return

307. Once registered a barrister will have to account quarterly for VAT. Virtually all VAT businesses have to file VAT Returns using compliant software (which is discussed above under "Making Tax Digital for VAT" at paragraphs 248 to 260) and pay electronically.

Information required

308. For the purpose of VAT accounting, the barrister will need to be given by their clerk the following information in relation to the relevant accounting period:

a. The amount of their gross receipts excluding VAT.
b. The amount of VAT charged.
c. The share of their deductible input tax from chambers, if any.
d. The total of their "taxable" professional expenses (excluding VAT) incurred during that period through chambers (i.e. those taxed for VAT at the standard rate and those which are zero rated).

309. They must also obtain from their own records:

a. Their deductible VAT from business expenses paid personally.
b. The total of their personal "taxable" (as in (d) above) professional expenses which they have personally incurred during that period.

310. They should also provide their clerk with details of the amount of any VAT paid in previous accounting periods which, for any reason, they have failed to pay and/or have overpaid, so that the clerk may use the appropriate error correction procedures, depending on the net amount involved in the error.

311. In general, where the net value of errors found on previous returns is below £10,000, it is possible to adjust the current VAT Return. For larger errors a special error

correction notification procedure using a special form VAT 652 [42] must be followed. In general there is a four year time limit for such adjustments or notifications and special advice should be taken in relation to errors discovered for out-of-time periods. Specific advice should be taken where it is proposed not to use VAT 652 to make a correction, as the penalty position is dependent upon it.[43]

What each clerk must record

312. All VAT registered barristers must account for VAT in relation to all professional services with which their clerks are likely to be concerned. Consequently they must levy 20% on the fee amount in respect of all work except that which is outside the scope of VAT. VAT registration applies to all business activities, so the records must contain details of other goods and services provided and VAT unless the goods and services are zero-rated, exempt or outside the scope of VAT. Sufficient and suitable records must be kept by all clerks, in accordance with the Making Tax Digital rules (see paragraphs 248-260) so as to enable them:

a. To record how much VAT output tax has been received by each of their principals.
b. To record how much input tax has been paid out by chambers generally on behalf of those principals.
c. To record chambers' taxable expenses whether zero-rated or not.
d. To inform those principals at suitable intervals of those amounts.
e. To divulge and demonstrate these records to Inspectors from HMRC if required.
f. To retain these records for a period of six years from each accounting period or for such less period as HMRC may allow.
g. To keep a VAT summary showing how much VAT those principals have paid.

Foreign currencies and the Euro

313. Invoices showing values computed in foreign currencies (including the Euro) must show the total net value of services and the total VAT payable in sterling. There are two methods. Unless a permitted alternative is adopted, the UK market selling rate must be used - the rates published in national newspapers are acceptable. As an alternative, certain rates of exchange published by HMRC for customs purposes may be used. If this option is adopted, it cannot then be changed without first obtaining

[42] https://www.gov.uk/government/publications/vat-notification-of-errors-in-vat-returns-vat-652

[43] Further general details are given in *VAT Notice 700/45/17* 'How to correct VAT errors and make adjustments and claims'.

agreement in writing. Applications in writing may be made for a different rate than the alternatives given.

Special Accounting Schemes

314. There are three special accounting schemes designed to assist "small" businesses as defined: the Annual Accounting Scheme (AAS), Flat Rate Scheme (FRS) and Cash Accounting Scheme (CAS).

a.) Annual Accounting Scheme

315. The first special scheme is an annual accounting scheme for small businesses (defined as those with an annual turnover of less than £1,350,000). Under this scheme a barrister is entitled to submit a single annual VAT return. Provided accounting records are properly maintained, kept up-to-date and not left until the year end, the scheme provides some simplification and, of course, removes the need for quarterly VAT returns. However, there is a different more onerous payment regime, in that regular instalments on account are required.

b.) Flat Rate Scheme

316. Businesses with a VAT-exclusive turnover of less than £150,000 can apply to be registered under the "flat-rate" scheme. A flat-rate scheme means (a) charging output tax as normal; (b) accounting for output tax at a reduced rate; (c) not recovering input tax. The purpose of the scheme is to reduce the administrative burden imposed when operating VAT. The scheme is optional and is open to businesses whose annual taxable turnover (not including VAT) does not exceed £150,000. Turnover for these purposes does not include the proceeds from the sale of capital assets. The turnover test applies to anticipated turnover in the following 12 months. This can be calculated in any reasonable way but would normally be based on the previous 12 months turnover. Businesses not already VAT registered may do so at the same time as applying to use the scheme. There is no penalty for exceeding the turnover limits but if the VAT inclusive turnover exceeds £230,000 the business must leave the scheme, unless it can be shown that total income in the next twelve months will not exceed £191,500.

317. Under the scheme a set percentage is applied to the turnover of the business as a one-off calculation instead of having to identify and record the VAT on each sale and purchase. There is no input tax deduction for purchases except capital assets valued over £2,000, inclusive of VAT.

318. The flat rate for barristers is dependent on whether they are a 'limited cost' business or not. If the barrister's business is a limited cost business, the flat rate

percentage will be 16.5%. This limited cost rule has applied since 1 April 2017. The calculation is complex and specific advice should be taken. It involves calculating relevant turnover as a proportion of cost of "relevant goods", not all goods being included, and services being excluded. If the amount spent on relevant goods (inclusive of VAT) is either less than 2% of turnover (as calculated under special rules for the flat rate scheme) or greater than 2% of turnover but less than £250 for a quarterly Return, then the business counts as limited cost.

319. Otherwise, the flat-rate which is applicable to barristers is 14.5% from 4 January 2011.

320. As the flat-rate is applied to the total of the fee plus VAT the saving in tax for a barrister on the 14.5% flat rate is therefore not 5.5% (as it might appear) but 2.6% of the net fee. This is shown as follows:

Fee	*Fee plus VAT*	*VAT*	*Flat rate output tax*
£1,000	*£1,200*	*£200*	*£174*

321. Thus, the VAT saving in output tax accounted to HMRC is £200-£174 = £26, or 2.6% of the fee. For a barrister on the flat rate of 16.5%, the saving would be £2.

322. It should be noted that there is a 1% discount on the flat-rate for the first year of VAT registration.

323. Barristers whose chambers use any of the methods of accounting for common expenses may use the scheme. However, those chambers using "the combination method" must follow special rules if they have any members using the flat-rate scheme. Furthermore, chambers must ensure that input tax claims are apportioned and only relate to those barristers who are not on the flat-rate scheme by additional record-keeping. This presents an administrative burden on chambers and results in the VAT related to those barristers on the flat-rate scheme not being recovered.

324. Whether it is beneficial for a barrister to adopt the flat rate scheme requires a detailed assessment of the likely saving in output VAT versus the loss of input tax recovery and if necessary, advice should be taken in considering this further.

Example

> *Maureen in LegalEagle chambers has annual fees of £60,000 and VATable expenses of £2,000 plus VAT. Her fee charges are £60,000 plus £12,000 of output VAT; her recoverable input tax is £400; she accounts to HMRC for (£12,000 – £400) = £11,600.*

Sebastian joins the flat-rate scheme, the applicable flat-rate being 14.5%. As before their fee charges are £72,000. He pays over to HMRC £72,000 x 14.5% = £10,440.

The net result is

	Normal	*Net-Normal*	*Flat-Rate*	*Net – Flat-rate*
Fees	*60,000*		*60,000*	
VAT	*12,000*		*12,000*	
Expenses	*(2,000)*		*(2,400)*	
Pay HMRC	*(11,600)*		*(10,440)*	
		58,400		*59,160*

The saving arises because Sebastian is allowed to keep part of the output tax, and this exceeds the amount of input tax which he could otherwise reclaim. On the other hand, an example could be produced just as easily demonstrating that the barrister loses by adopting the scheme due to the VAT on expenditure exceeding the reduction in tax due on income. This would be particularly relevant to the leading advocate under a fee-sharing protocol where VAT is charged on the invoice from the "sub-contracted" barrister.

Records and invoicing/income tax

325. A record of the flat-rate calculation showing the flat-rate turnover for the accounting period, the flat-rate percentage used, and the tax calculated as due must be kept with the VAT account.

326. Invoices for clients will still need to be shown at the standard rate of 20%.

327. For income tax purposes barristers using the scheme should prepare accounts using earnings inclusive of VAT (gross receipts, again inclusive of VAT, if on cash basis) less flat-rate VAT applying the relevant percentage. Expenses will include the irrecoverable input VAT.

Pros and cons of the flat-rate scheme

328. The scheme offers a simplified expedient procedure for dealing with VAT. Those interested in taking up the scheme should identify whether it is suitable for them and whether or not an advantage accrues.

329. Method 3 (the combination method) accounting does mean that there is an additional burden on their chambers where members use the flat-rate scheme.

330. The flat-rate scheme can be used in conjunction with the annual accounting scheme requiring a single annual return. This could save time and money.

331. It is important to note that the flat-rate applies to all the supplies the barrister makes, including the value of exempt supplies, such as rental income from buy-to-let property or the sale of such a property. As exempt and zero-rated supplies are included in the flat rate turnover, it is possible depending on circumstances to pay more VAT by being on the scheme.

c.) Cash Accounting Scheme

332. Using cash accounting, VAT is accounted for to HMRC each quarter on the basis of payments received and made (rather than by reference to the tax point of supplies made and received). In other words, a business does not need to pay VAT until its own clients have paid up and conversely, VAT on expenses cannot be reclaimed until settled.

333. This scheme is generally available to businesses, provided that the annual taxable turnover is expected to be less than £1.35 million (excluding VAT and capital items). After joining, a barrister can remain in the scheme until the annual taxable turnover exceeds £1.6m. "Outside the scope" supplies are disregarded for the purposes of the threshold tests.

334. The scheme tends not to be used by barristers as they will normally only have to account for VAT on receipt of the fee under the special rules for barristers.

335. Using cash accounting, VAT is paid on sales when customers pay; VAT is recoverable on purchases only when suppliers have been paid. This may be helpful for cash flow, especially if recipients of the particular barristers' services are slow payers. Indeed, if the recipient never pays, VAT will not be due on that bad debt so long as the cash accounting scheme continues to be used.

336. On the other hand, the following disadvantages should be noted:

a. the VAT cannot be reclaimed on purchases until they have been paid for. Where most purchases involve credit, this may be disadvantageous, and

b. similarly in circumstances involving settlement on deferred payment terms, under cash accounting the input VAT reclaim will normally fall later.

337. On leaving the cash accounting scheme, account will have to be made for all outstanding VAT due including any bad debts.

338. Cash accounting cannot be used:

a. By anyone in default on their VAT obligations.
b. In relation to purchases or sales involving leasing, hiring, conditional or credit sales.
c. Importing goods into Northern Ireland from the EU.
d. Where the payment terms of a VAT invoice are 6 months or more.
e. In relation to invoices issued in advance services rendered.
f. In relation to the users of the flat rate scheme.

339. There is no need to complete an application form or advise HMRC to start using cash accounting. It is possible to start at the beginning of any VAT period for barristers already registered for VAT; and, in other cases, from the day the VAT registration commences.

340. It should be noted that those already registered should take care that they do not account for VAT twice on any sales or purchasing. It is necessary to identify and separate any transactions in existing records where account has been rendered for them using the standard procedures.

Joining and leaving the cash accounting scheme

341. The scheme can be left at the end of any VAT accounting quarter. It does not need to be notified to HMRC. As discussed above, the scheme ceases to be available where the taxable turnover is over £1.6 million.

342. Broadly, on leaving the cash accounting scheme, account has to be made for all outstanding VAT due, save for a deferment option of up to 6 months on uncollected amounts subject to conditions.

Penalties for late VAT returns

Up to 31 December 2022

343. If a taxable person is in default in sending in their VAT return and/or making payment of the VAT shown as due for the period, HMRC will serve a surcharge liability notice. The notice is a warning that a penalty will be imposed if they default again within a period ending one year after the last day of the accounting period for which the tax was due. This period is known as the "notice period." The penalty for the first default following the issue of a surcharge liability notice is 2%. In addition, to

the penalty, the notice period is extended to the anniversary of the last day of the prescribed accounting period for which the return was late, or tax was not paid.

344. Further default will result in increased penalties and further extensions of the notice period. The rate of penalties is:

Default	
First	*Warning notice*
Second	*2% of tax due*
Third	*5% of tax due*
Fourth	*10% of tax due*
Fifth and subsequent defaults	*15% of tax due*

345. If on a default no tax is due, there is no penalty, but the notice period will be extended.

346. A prescribed percentage penalty can be avoided by showing that there is a "reasonable excuse", but reliance on a third party (e.g., a clerk) or insufficiency of funds will not usually constitute a reasonable excuse.[44]

From 1 January 2023 [45]

347. A new penalty regime comes into force, based on a points system. A late quarterly return will result in 1 penalty point and once 4 penalty points have been exceeded (the penalty threshold) there will be a £200 penalty for each subsequent late return.

348. Points expire after two years but not if the barrister is at the penalty threshold. If at the penalty threshold the points can only be reset when both of two conditions are satisfied: (1) the barrister has submitted all returns on time for a period of twelve months and (2) all of the submissions due for the preceding twenty-four months have been submitted (it does not matter if a submission was late).

349. There are penalties for late payment. There is no penalty if the VAT is paid up to 15 days late. A penalty of 2% applies to the VAT due at day 15 plus 2% to the VAT owed at day 30. For VAT outstanding at day 31, a further penalty will accrue on a daily basis for the duration of the outstanding balance at a rate of 4% per year.

350. It will be possible to avoid penalties if there is a reasonable excuse

[44] See section 71 (1) of VATA 1994.

[45] The introduction of a new penalty regime was deferred from 1 April 2022 to 1 January 2023 and readers should check that there has not been a further postponement.

351. Late interest will also be charged on late payment calculated at the Bank of England base rate plus 2.5%

Part Seven: Discontinuance of Practice at the Bar - The Tax Position

352. On discontinuance of practice, either on retirement (including taking a full-time judicial appointment, but not taking silk) or on death, a number of major issues need to be considered. The most important are:

a. The tax liability arising from the final period in practice, where a number of adjustments need to be made.
b. The tax position in respect of post-cessation adjustments, both receipts and payments.
c. Other matters:
    i. VAT, or
    ii. Professional indemnity insurance.

Tax position on final accounts

353. It is assumed the barrister will always keep to the same accounting date. They can of course change their accounting date any time they wish, but if they do so extra complications, not dealt with here, are likely to arise.

354. When you cease practice, the profits assessable in the final tax year (whether calculated under the cash basis or earnings basis) of your practice will be those arising in the period beginning immediately after the end of the basis period for the preceding year and ending on the date of cessation.[46] This period may be more than twelve months. Where overlap relief has arisen on commencement this is available to offset against the profits assessable in the final period.

355. The following illustration may be of interest:

> *Matthew ceases to practice on 30 June 2021. He has always prepared accounts to 31 March each year and they show a profit of £115,000 for the year to 31 March 2021 and his profits for the final three months are £45,000.*
>
> | | |
> |---|---|
> | *2020/2021* | *£115,000* |
> | *2021/2022* | *£45,000* |
>
> *Felicity ceases to practice on 30 June 2021. She has always prepared accounts to 30 April each year and they show a profit of £115,000 for the year to 30 April 2021 and her profits for the final two months are £23,000.*

[46] See section 202 of the Income Tax (Trading and Other Income) Act 2005.

2021/2022	*£*
Profits for 14 month period of cessation	*138,000*
Less: assumed overlap relief	*8,383*
	£129,617

356. As can be seen from the examples above there can be large differences in the amount of profit being assessed to tax in the final year. Matthew above is required to pay tax on a final year profit of £45,000 whereas Felicity is required to pay tax on a final profit of £129,617. The reason for the large difference is clearly because Matthew is required to pay tax on three months' profits whereas Felicity is required to pay on 14 months (less a small amount of overlap relief). Felicity has, however, had the advantage throughout her career of paying tax in arrears on what was generally speaking a rising income. Matthew, however, was paying tax very much on an actual basis. Whilst some of Felicity's profit was doubly assessed to tax in the second year of practice, hence giving rise to some overlap relief, such relief is likely to be small when compared to the final year profits. This is simply because profits would have been small in the first years of practice and much larger in the final years. Those worse affected on cessation will be those with an accounting period ending shortly after 5 April (for example, 30 April), whilst those least affected, will be those with an accounting period ending on 5 April or close to (i.e., 31 March).

357. It is therefore especially important that someone with an accounting period ending shortly after 5 April is aware of the position and makes due provision by maintaining an adequate tax reserve.

358. It should also be recognised that this aggregation of profits can lead to part of the profits falling into a higher tax bracket compared to the position for just 12 months' profits. Barristers wishing to avoid assessability on more than 12 months profits (less overlap relief) on retirement should arrange (where possible) to retire on a date after 5 April.

Example

> *Stephen prepares accounts to 30 April each year and retires on 10 April 2021. Assessments will be:*
>
> *2020/2021 - 12 months to 30 April 2020*
> *2021/2022 – period 1 May 2020 to 10 April 2021*
>
> *By contrast, if retirement had occurred on 5 April 2021, all the profits would have been assessable in 20120/2021.*

359. The proposal to end the 'Current Year Basis' of assessment to a 'Tax Year' basis (see paragraph 64) should result in the end of this aggregation of profits with effect from 2023/24.

Maintenance of a tax reserve

360. It is not easy to establish a tax reserve. Early in a barrister's career other demands on their cash resources often make it impracticable to set money aside for future tax payments. Similarly, a barrister in mid-career who does not have a tax reserve is hard-pressed to create one, since much of the current year's profits goes to pay the current tax bills.

361. Nevertheless, many barristers do maintain tax reserves, and they are plainly in a much better position to sustain the tax costs of a cessation after periods of rising profits. Their tax reserves will cover any extra tax arising and, even after payment of that, some of the reserves may not be needed to pay tax liabilities and will provide welcome uncommitted cash resources.

362. All barristers are recommended to do whatever they can to establish, out of current receipts, reserves to meet future tax liabilities. Following the cessation of a barrister's practice, tax payments will continue to become due for a period currently extending as long as 21 months for a 30 April year end (9 months from 2023/24 if the Tax Year basis applies). These may form a considerable burden if adequate provision has not been made to build up tax reserves out of current receipts.

Terminal loss relief

363. Relief may be claimed to set a loss incurred in the final 12 months of practice against the practice income of the tax year of cessation and the three previous tax years. The terminal loss may include any available overlap relief.

Adjustments on final accounts on earnings basis

364. If the earnings basis applies a number of adjustments need to be made in the final accounts:

a. A more critical assessment of the value of outstanding fees is advisable.
b. Any future liability for the payment of chambers rent after cessation should be brought into account. And,
c. Any future liability for the payment of clerks' fees after cessation should be brought into account.

365. For those assets still held on which capital allowances have been claimed on discontinuance, the "disposal value" of any assets still held on which capital allowances have been claimed, is brought into account. If the written-down value in the pool exceeds the disposal value, a balancing allowance is given equal to the difference. If disposal value exceeds written-down value, there is a balancing charge on the excess. "Disposal value" means sale price or, if there is no sale, market value, but disposal value cannot exceed original cost.

Outstanding fees at cessation

366. For those preparing final accounts on the earnings basis the most important item, which is a matter of judgement in individual cases, is the assessment of the value of outstanding fees (billed and unbilled but not received by the time final accounts are prepared). It is almost certain that the amount ultimately received will be greater or lesser than the figure included in the final accounts. Any difference, either greater or lesser, needs to be accounted for in future tax returns. These adjustments are dealt with as follows:

a. Where the figure received in total is greater, the surplus must be declared in the tax return covering the year in which the surplus arose. It is possible that such a declaration may need to be made in more than just one return. For example: a barrister retired on 30 June 2020 with outstanding fees owed of £87,000. It was considered that some fees may not be paid at all, and that a reduced sum might be paid on others, especially those subject to Legal Aid taxation. After due consideration the barrister decided that a fair and prudent assessment of what the barrister might ultimately obtain was £65,000. By 5 April 2021 the barrister had received £58,000. During the year to 5 April 2022 the barrister received a further £11,000. On the tax return to 5 April 2022 the barrister would have to declare, as miscellaneous income, the "windfall" profit of £4,000 (£58,000 plus £11,000 less £65,000). If any further monies are received in future years those would also have to be returned on a future tax return(s). Alternatively, surplus receipts received in a tax year beginning no later than six years after the date of cessation may, on election, be treated as received at the date of cessation. This may be of benefit if the tax rate applying to the barrister in the year of receipt is greater than that in the year of cessation. Effect is given to the election by an adjustment to the tax return of receipt, and

b. Where the figure received in total is lesser, relief can be claimed for the shortfall. Using the example under (a) if by, say, 5 April 2022 the £58,000 received to 5 April 2021 is known to be all that will be received, then the barrister has paid tax on £7,000 more profit than actually made. On the tax

return to 5 April 2022 the barrister can make a claim for relief for this sum against their other income for 2021/2022.

Practical issues to be considered regarding outstanding fees

367. Whilst there is no time limit for declaring any "windfall" profit, a claim for relief in respect of any shortfall must be made within seven years of the profession ceasing. This seems unfair, and so the advice must be that on assessing the amount that is likely to be received for fees owing at cessation, a particularly prudent approach should be adopted.

368. It is quite possible that relief for any shortfall will be at a lesser tax rate than was originally paid on the figure; dependent on the retired barrister's tax rate in the year the claim is made. Provided the figure is known by 31 January, 21 months after the tax year of cessation, it may be advisable to make an amendment to the tax return covering the year of cessation. In this way there is no danger of receiving relief at a lesser tax rate (i.e., where cessation happened on 30 June 2021 an amendment to the tax return for the year of cessation, 2021/2022, can be made by 31 January 2024).

369. Relief against post cessation receipts is allowed for expenses, such as clerk's fees, falling due to be paid as outstanding fees are received, to the extent that they exceed the amount provided for in the final accounts.

Cash basis

370. If the cash basis applies, the value of any Work in Progress[47] at the time of the cessation is brought into account as a deemed receipt in calculating the profit. It is difficult to envisage any significant work in progress for a typical retiring barrister, as inevitably it will have been "billed". Nonetheless, it is required to be considered and brought into account where relevant. By contrast fees received after cessation are taxed as post cessation receipts except to the extent that they are already included in closing work in progress.

371. Relief against post cessation receipts is allowed for expenses, such as clerk's fees, falling due to be paid as outstanding fees are received, to the extent that they exceed the amount provided for in the final accounts.

[47] Work in progress on cessation means: services performed in the ordinary course of the profession… the performance of which is wholly or partly completed at the time of cessation, and for which it would be reasonable to expect that a charge would be made if there were no cessation and, in the case of partly completed services, their performance were fully completed (Section 183 ITTOIA 2005).

Old cash basis

372. Although not now generally applicable since it has been phased out since 2013, it is mentioned for reference that for those on the "old" cash basis (which was a special basis of cash accounting available to barristers only), a post cessation receipt is taxable as miscellaneous income.

373. Relief against post cessation receipts is allowed for expenses, such as clerk's fees, falling due to be paid as outstanding fees are received, to the extent that they exceed the amount provided for in the final accounts.

Catch up charge

374. Historically, the change from the old cash basis to the earnings basis resulted in adjustment income which could be spread and taxed over 10 years. If a barrister retired within the 10 years, he or she could continue to take advantage of the spreading provisions. Hence, post cessation, the adjustment income continued to be charged each tax year over the remaining years of the spreading period, until the tenth year, when the balance of the adjustment income became taxable. The figure needs to be declared on the tax return as miscellaneous income.

Cash Basis

375. For barristers changing from the cash basis to the earnings basis, any "adjustment income" on changing is spread over six years. If a barrister retires within these 6 years, he or she can continue to take advantage of the spreading provisions.

VAT

376. A barrister is normally accountable for Value Added Tax (VAT) on their fees when the fees are paid. HMRC state in *Notice 700/44* ("Barristers and advocates") that on discontinuance, the normal position is that VAT is accountable on all outstanding fees. However, HMRC allow by permission retired members of the Bar to defer payment of VAT on outstanding fees until the fees are paid, or if earlier, a VAT invoice is issued. The relevant VAT rate will be that in force at the date of cessation. This permission must be applied for; the current VAT Notice referred to states that it needs to be done by letter. A letter attachment may not be possible with online VAT deregistration; and the appropriate procedure will need to be specifically examined at the time.[48]

[48] See HMRCs leaflet 700/44 which details the procedures to be followed.

377. Retirement involves de-registration, and on de-registration, a barrister is treated as making a supply of any assets that they still own and for which they have taken a credit for input tax (e.g., carpets, furniture, computers). The supply is treated as made for a price equal to the second-hand value of the assets. Books are zero-rated so this rule has no application to law reports, nor does it apply to antiques bought from a dealer operating the special scheme for dealers under which they apportion VAT on their margin but no input tax is allowed to the purchaser.

Professional indemnity insurance considerations

378. The Bar Mutual Indemnity Fund (BMIF) provides, free of charge cessation cover of £500,000 from the date of retirement. Additional cover can be purchased up to a maximum of the cover applying during the three years to retirement.[49] A barrister should consult the BMIF in good time before cessation and consider carefully whether additional cover may be needed.

379. There is free of charge cover on death for six years at the cover limit pertaining on death. Bar Mutual should be informed of the death as soon as practicable.

380. Generally, a premium paid for excess run-off cover should be deductible against the final profits.

381. HMRC expresses the view that...

> *...premiums paid after cessation can be relieved against post cessation receipts; and that they would not seek to disallow premiums paid whilst in practice where the cover extends to claims lodged after cessation.*[50]

[49] https://www.barmutual.co.uk/insurance-cover/special-circumstances/

[50] HMRC, October 1995, Revenue Tax Bulletin.

Part Eight: Self Assessment

382. Under self assessment a barrister must calculate their own tax liability and ensure the tax is paid on time. Even when an accountant is engaged to deal with these matters, responsibility for self assessment remains with the barrister.

383. The barrister will receive a tax return designed to disclose their income and capital gains and enable them to calculate their tax liability. This tax is due on set dates each year. Interest and penalties are charged where returns or payments are late.

384. The return consists of core pages that are common to every taxpayer. For barristers, this is supplemented by the six self-employment pages in which they disclose their professional profits and expenses.

385. If their annual turnover, (i.e. receipts/earnings before deductions) is less than the Value Added Tax (VAT) registration threshold (currently £85,000), the only details they need provide are the turnover and expenses.

386. If the turnover is above this figure, the form requires the recasting of the barrister's accounts information in a standard layout which is used by HMRC for their risk assessment procedures.

387. HMRC publish a number of help sheets and explanatory pages which together should be reviewed before the return is filled in.

388. In order to reduce the possibility of HMRC opening an enquiry into a return, it is worth ensuring that:

a. In each year's return expenses are put under the same head, for example, professional subscriptions should not be switched between such categories as "general administrative expenses" one year and "other expenses" the next, and

b. If accounts are prepared so that the proportions of expenditure representing private use are excluded, those figures can be used on the return without the gross equivalent but it is advisable that a note be added on the return explaining that this has been done.

389. In order to assess the tax liability there are two alternative procedures from which the barrister is able to choose:

a. Submission of the paper return manually by 31 October following the end of the tax year (or two months after the issue of the return if later). In this case HMRC will calculate the tax position, or

b. Submission of the return electronically by 31 January following the end of the tax year (or within three months of the date of issue of the return if later). This is known as the filing date. In this case the taxpayer must assess their own tax liability and the amount of tax due must be shown on the return.

390. If the self assessment return is not filed on time, there is an automatic penalty of £100. If the return is still not submitted after a further 90 days HMRC can impose a daily penalty of £10 for each day that the failure continues. If the failure continues after six months from the filing date, there is a liability to a penalty equal to the greater of £300 and 5% of any tax liability which would have been shown in the return in question. There is a right of appeal if the taxpayer has a reasonable excuse for late submission, but this only covers circumstances beyond the taxpayer's control, such as unforeseen illness. Furthermore, there are provisions for further tax geared penalties if the failure continues for 12 months from the filing date.

391. After the return is filed, HMRC have nine months from the date the return is filed to correct any obvious errors or mistakes on the return. The taxpayer has a similar right, but has 12 months from the filing date as long as HMRC have not started an enquiry. The filing date being 31 January following the tax year to which the return relates.

392. HMRC will select returns for enquiry each year and can issue a notice to this effect up to 12 months after the date the return was filed or, if the return is filed late, by the quarter-day following the first anniversary of the date of delivery or amendment to the return. A notice is sent to the taxpayer, and if they are represented, to their agent.

Payment of tax

393. For this purpose, tax includes Class 4 and Class 2 National Insurance Contributions (NICs). However, the payment of the Class 2 NIC is made in full on 31 January each year and does not form a part of the payments on account.

394. Income tax will generally be due in two equal instalments: on 31 January during the tax year, and 31 July after the end of the tax year. The amount of each of these instalments is half the liability of the previous year excluding Class 2 NIC and capital gains tax. The balancing tax together with Class 2 NIC and tax on capital gains is payable on 31 January after the end of the tax year.

395. Provisions exist for claiming reduced instalment payments if the taxpayer anticipates the liability for that year will be less than the liability for the previous year. However, interest is charged on any underpayment by reference to the instalments that would otherwise have been payable.

396. Where the payments on account exceed the liability for the year, the excess may be refunded or set off against future tax instalments.

397. Interest is charged on the late payment of tax. Such interest is not tax deductible. Furthermore, a 5% late payment penalty arises in respect of the balancing tax and any capital gains tax unpaid after 30 days. There is a further 5% penalty on tax still unpaid after six months and yet another 5% penalty if the tax is unpaid after 12 months.

Example

For an established barrister
Tax year 2021/22

31 January 2022	*First instalment*
31 July 2022	*Second instalment*
31 January 2023	*Balance of tax due, or refund of excess of instalment payments over the liability, if not made earlier*

Income tax overlap relief

398. It is a basic principle of self assessment that over the lifetime of the profession, all of the profits will be charged to tax; none of the profits will fall out of charge and if any profits are charged to tax more than once, appropriate relief is given.

399. In the early years of a barrister commencing in practice, it is possible for profits to be assessed more than once and so overlap relief is created as discussed in Part Two of this guidance.

400. There is, however, a further form of overlap which was established on the commencement of self assessment referred to as "transitional overlap relief." This is defined as the amount of profits, before capital allowances which were taxed in the 1997/98 tax year but which arose prior to 6 April 1997. Where applicable, the transitional overlap would have already been established and should appear at box 70 on the full Self Employment supplementary pages to the self assessment tax return.

401. Overlap relief (of both types) is frozen and is carried forward and deducted from profits in the final year of the profession.

402. Overlap relief can be used earlier by extending a barrister's accounting period to a date closer to the end of the tax year. A proportion of the overlap relief representing a period in excess of one year would then be available as a deduction. It is worth bearing this in mind as a barrister approaches retirement and finds that their earnings are reducing. If they have traditionally paid tax at higher rates they should also consider changing their accounting date if it might otherwise mean that the relief would only be available at the lower rate. On the basis that the relief is not index-linked, barristers may also consider changing their accounting date to make use of the relief while its inherent value is greater.

Part Nine: Retirement Provision for Barristers

403. As self-employed persons, barristers face the responsibility of making their own retirement provision. What follows deals with pensions, which are the main vehicle for retirement planning because of their favourable tax treatment. However, there are restrictions on the amount one can invest in pensions and higher earners should consider supplementing their pensions with other forms of savings.

404. On 1 July 1988, Personal Pension Plans (PPPs) replaced Retirement Annuity Contracts (RACs). This means that no new RAC contracts can be effected after 1 July 1988, but existing RAC contracts may continue and in most cases it is possible to increase the premiums without effecting a new policy. From 6 April 2006 both types of policy are subject to the new rules governing registered pension schemes.

Pension contributions and tax relief

Net Relevant Earnings

405. Pension contributions are calculated by reference to Net Relevant Earnings (NRE). These are earnings arising from self-employment, either alone or in partnership, less allowable expenses. In brief this is the profit figure less capital allowances plus, where applicable, the "catch-up" charge.

Tax Relief

406. Your pension provider will automatically claim basic rate (currently 20%) tax relief 'at source' – this means that when you pay some personal pension contributions into your pension plan, some additional money is added on top of this by the government.

> As an example, if you make £80 of personal pension contributions, the government adds another £20 to your pension, making it £100 in total.
>
> The £80 (how much you pay in) is called your 'net' contribution – when this is combined with the £20 top up from the government the total £100 is called the 'gross' pension contribution.

When it comes to your personal tax return, your gross pension contributions have the effect of increasing your basic rate tax band which means you will save some tax through your tax return if your earnings are in the higher tax band or above. This tax saving will be deducted from your tax charge.

Lifetime Allowance

407. From 6 April 2006 the total value of all an individual's tax privileged pensions must fall below a new limit, known as the Lifetime Allowance (LTA) also known as the Standard Lifetime Allowance (SLA). Any excess over the lifetime allowance. The lifetime Allowance was introduced on 6 April 2006 (A-Day) but has not remained at the same level. At the time of writing, it is currently £1,073,100. The Spring Budget of 2021 announced that the lifetime allowance would be frozen at £1,073,100 until April 2026 at the earliest.

408. In some circumstances an individual's lifetime allowance will actually be higher than the standard lifetime allowance, as they may have benefited from one of the following "protections":

a. Primary Protection – protection is given to the value of pre "A-Day" (5 April 2006) pension rights and benefits in excess of £1.5m. The pre A-Day value will be indexed in parallel with the indexation of the statutory lifetime allowance up to the date that benefits are taken. It is possible to accrue "Relevant Benefit Accrual" post A-Day. To be able to elect for Primary Protection, an individual's A-day value must have exceeded £1.5m, or

b. Enhanced Protection – this was available to individuals who ceased all "Relevant Benefit Accrual" after 5 April 2006. There is no requirement for the A-Day value of their benefits to have been greater than £1.5m.

In both of these cases the barrister must have registered with HMRC by 5 April 2009.

409. Fixed Protection - if a barrister did not have either primary or enhanced protection, then "Fixed Protection" could have been applied for. A barrister may still be able to claim Fixed Protection (provided that no pension contributions or benefit accrual since 6 April 2016).

The lifetime allowance was steadily reduced from its high point of £1.8 million in 2010/11 until it was linked to the CPI from 2018/19.

Each time it was reduced, fixed protection was made available to allow the member to retain the previous lifetime allowance. However, any contributions or benefit accrual results in the loss of fixed protection. Some transfers also result in the loss of fixed protection.

- Fixed protection 2012 gives protection of £1.8 million

- Fixed protection 2014 gives protection of £1.5 million
- Fixed protection 2016 gives protection of £1.25 million

Fixed protection 2016 is the only one you can still apply for and there is no time limit for applications.

410. Individual Protection

This allows a protected lifetime allowance up to the capped value of total pension savings at a certain date.

Individual protection 2014 provides protection up to the lower of the value of total pension savings at 5 April 2014 and £1.5 million. Barristers could apply for it if their pension savings were worth at least £1.25 million at that date.

Individual protection 2016 provides protection equal to the lower of the value of total pension savings at 5 April 2016 and £1.25 million. Pension savings had to be worth at least £1 million at that date.

Further contributions, benefit accrual or transfers do not result in the loss of individual protection 2014 or individual protection 2016.

Barristers can still apply for Individual Protection 2016; there's no time limit for applications.

Contribution Limits pre-6 April 2006

411. Prior to 6 April 2001, the maximum aggregate contributions which a barrister could pay into an approved pension contract depended on their age at the beginning of the year of assessment in which contribution was to be relieved.

412. From 6 April 2001, maximum contributions continued to be determined by percentages of Net Relevant Earnings and the earnings cap, but the "earnings" employed in the calculation did not have to be current year earnings. Instead, barristers could nominate any of the previous five tax years as their "basis year" (a basis year could have been before 2000/01). The percentage, however, was always related to current age. Eligibility to contribute was also extended: contributions of up to £3,600 per annum gross could be made without the need for any NRE to justify the contribution.

Contribution Limits Post 5 April 2006 until 5 April 2011

413. Individuals could contribute up to the higher of £3,600 gross and 100% of relevant UK earnings. However, there was a single limit on the tax-advantaged contributions that could be paid each year into pension schemes by an individual. This limit was known as the "annual allowance." The annual allowance for the tax year 2006/07 was set at £215,000, increasing by £10,000 each tax year to £255,000 in the tax year 2010/2011. If contributions exceeded the annual allowance, then the individual was taxed on the excess, via the annual allowance charge.

Contribution Limits Post 5 April 2011 and Carry Forward of Unused Annual Allowance

414. The annual allowance of £255,000 was reduced to £50,000 on 6 April 2011 and has been reduced further to £40,000 from 6 April 2014. Where an individual's pension savings exceed the Annual Allowance for a tax year, a tax charge may apply.

415. However, it is now possible for to "carry forward" any unused allowance from the three previous tax years, provided the individual has been a member of a registered pension scheme in each of those years – this includes where a barrister may have established a pension arrangement a number of years before with a single contribution and made no further pension savings in the intervening years.

Tapered Annual Allowance

416. The tapered annual allowance rules came into force on 6 April 2016 to limit the amount of tax relief high earners could get on their pension contributions.

The taper works by reducing the annual allowance by £1 for every £2 of adjusted income above the 'adjusted income' limit, assuming that the individual has exceeded the 'threshold income'.

Adjusted Income - Broadly, it includes all taxable income and all pension savings less certain reliefs.

Threshold Income - In simple terms, it's a person's income but without adding back in any employer pension contributions.

The taper works by operating a £1 reduction in the annual allowance for every £2 of adjusted income above £240,000, subject to a minimum annual allowance of £4,000. So, those with an adjusted income of £312,000 or more in a tax year will have a £4,000 annual allowance for that tax year.

However, if an individual's 'threshold income' is no more than £200,000 they will not be subject to the tapered annual allowance."

Payment of premiums

417. The premiums can be paid by means of regular contributions or by a series of single contributions. The latter method is advantageous since it provides flexibility in terms of the amount to be paid.

Combining a Personal Pension Plan with life assurance

418. Pension Term Assurance (PTA) is standard term life insurance but with premiums that attract tax relief so the net cost could be cheaper. However, in respect of PTA policies linked to Personal Pension Plans, tax relief is no longer available for contributions made on or after 6 April 2007 in respect of PTA policies, unless the insurer received the policy application before 14 December 2006 and the policy was taken out before 6 April 2007.

419. Tax relief on premiums for policies that continue to qualify will be stopped if the policy is varied to increase the sum assured or extend the term, unless the variation is as a result of the exercise of an option within the policy.

Death benefits before retirement

420. Before 6 April 2015 what benefits could be paid depended on whether the funds were crystallised or not. Since 6 April 2015 it is the age of person who dies at their date of death that affects the tax treatment of the benefits, there is no different for crystallised and uncrystallised funds. However, a lifetime allowance check applies to uncrystallised benefits.

421. Uncrystallised funds:

- Death before 75 - The fund can be paid to any beneficiary completely tax-free as a lump sum, annuity or as a drawdown pension. The benefits will be tested against the lifetime allowance.

- Death after 75 – The fund can be paid to any beneficiary, taxed at their marginal rate, as a lump sum, annuity or as a drawdown pension. The fund can be paid to a trust as a lump sum less a 45% tax charge.

422. Crystallised funds

- Death before 75 - Can pass on completely tax-free to any beneficiary as a lump sum or as a drawdown pension. A drawdown fund can be used to buy an annuity at any time.

- Death after 75 - The fund can be paid to any beneficiary, taxed at their marginal rate, as a lump sum, annuity or as a drawdown pension. The fund can be paid to a trust as a lump sum less a 45% tax charge.

423. It will generally be advisable for barristers to have their pensions written in trust (for members of their families) for Inheritance Tax (IHT) purposes, but advice must be sought depending on the individual's circumstances.

Benefits at retirement

Retirement age

424. Subject to the terms of the policy, the benefits from a personal pension can be taken at any time from the age of 55, irrespective of whether or not the barrister has actually retired. This will increase to 57 in 2028.

It is possible for pension benefits to be taken where a member is in ill-health or serious ill-health. Pension benefits can be taken earlier than age 55 due to ill-health whilst benefits can be taken as a lump sum due to serious ill-health at any age.

Tax-free lump sum

425. Under a personal pension, up to 25% of the pension fund can be taken as a tax-free lump sum on the chosen retirement date, up to the value of the lifetime allowance. This payment is referred to as the Pension Commencement Lump Sum (PCLS).

426. An individual may have accrued occupational scheme benefits prior to joining the Bar, in this instance they may have the right to take more than 25% of the value of the pension accrued as a tax-free sum and these rights will be automatically retained within that pension scheme. If benefits are individually transferred away from the scheme the 25% limit will apply and the protection of lump sum rights is lost.

Annuities

427. The pension fund can be used to purchase an annuity which is in effect the pension. Most pension providers offer an open market option that enables the barrister to transfer pension funds to whichever insurance company is offering the best annuity rates at the time.

428. It can then be decided which of the various types of pension/annuity is best suited to the individual's requirements.

429. As a result of falling interest rates and increasing longevity, there has been a sharp decrease in annuity rates in recent years. The Finance Act 1995 introduced income withdrawal which is an alternative method of taking retirement benefits.

Drawdown Pension (previously known as Unsecured Pension/Income Withdrawal/Income Drawdown)

430. This provision was originally designed to allow an individual to draw income from their pension fund without purchasing an annuity.

431. From 6 April 2015, from age 55, individuals can access as much of their savings from their defined contributions pension scheme (also known as 'money purchase schemes') as they want under new 'pensions flexibility' rules.

Flexi-access Drawdown (FAD)

432. Flexi-access drawdown pension replaced flexible drawdown on 6 April 2015.

433. Using flexi-access drawdown, a pension holder can crystallise their pension fund, usually taking up to 25% of it as a Pension Commencement Lump Sum (PCLS) while the balance of the money continues to be invested (please note these funds are now crystallised funds).

Uncrystallised funds pension lump sums (UFPLS)

434. Uncrystallised funds pension lump sums (UFPLS) are a way of taking pension benefits from money purchase pensions without going into drawdown or buying a lifetime annuity.

435. Under the UFPLS option, an individual can take their uncrystallised pension funds in one go, or as a series of lump sums.

Capped Drawdown

436. Capped drawdown is a form of income withdrawal. The maximum income which can be taken in a pension year is calculated by the Government Actuary's Department. Income taken can't exceed this limit, but the amount of income taken can be varied from year to year.

437. Any capped drawdown arrangements in existence before 6 April 2015 (with pre-6 April 2015 funds in them) continued unchanged when the pension flexibility rules were introduced on 6 April 2015.

438. New capped drawdown arrangements (including dependants' capped drawdown arrangements) can't be created after 5 April 2015 unless it's to accept a capped drawdown to capped drawdown transfer.

439. Drawdown is likely to be most effective for barristers who have a fund of at least £100,000 and who are prepared to accept some investment risk in retirement. The advantage is that it allows flexibility in the timing of the purchase of the annuity to avoid having to secure an annuity when rates may be very low, allowing the barrister to retain control over their pension funds for as long as possible.

Types of pension

Standard Personal Pensions

440. These are offered by most large pension providers. They're likely to offer a broad range of investment choices in the shape of unit linked funds.

Stakeholder Pensions

441. These allow you to make low minimum contributions. You can stop and start payments and transfer out at no cost. Annual charges are capped, although they're not always lower than some other pensions.

Under current legislation stakeholder pensions must offer certain features, including penalty free transfers, no initial charge, and a cap of 1.5% for ten years and 1% thereafter in respect of annual management charges. Whilst these are also a feature of personal pensions, they are not subject to the same legislative requirements and the providers could increase the charges or impose exit penalties in respect of their personal pension contracts at any time.

Self Invested Personal Pension Schemes

442. Self Invested Personal Pension Schemes (SIPPs) were introduced on 11 October 1989 to give members a wider degree of investment choice, including the ability to determine what assets should be held and when they should be bought or sold. The rules offer access to a wide range of assets that may be held in a SIPP, but barristers may be most interested in the option to invest directly into the stock market.

443. In addition, a large number of barristers have used SIPPs as a mechanism for purchasing their own chambers premises in a tax-efficient manner. Not only will the rental income paid by tenants and members be added to the SIPP without any deduction for income tax, any appreciation in the value of the chambers building will also be free from capital gains tax.

The importance of making a pension provision

444. All being well, barristers will be in retirement for over twenty years and will need to accumulate a substantial amount of money in order to provide for a good standard of living.

445. One of the best features of using a pension to save for retirement is tax relief. When paying into your pension, some of the money that would have gone to the government as tax goes towards the pension instead. This can help reduce the amount of tax the barrister pays and be used to help bolster savings for the future.

446. It is important to review pension contributions on an ongoing basis, taking into account personal circumstances, and ideally make substantial pension contributions each year, if possible. It is also important to increase the contributions at least in line with inflation. To determine what appears to be a reasonable contribution in one year and then simply to continue paying the same amount each year will inevitably lead to an inadequate pension.

Part Ten: Entities

447. If a barrister sets up an entity that will supply legal services to the public, that entity will need to be regulated.[51] There are two types of types of entity that the Bar Standards Board (BSB) can authorise:[52]

- BSB Authorised Bodies: barrister only bodies, fully owned and managed by barristers.

- BSB Licenced Bodies: also referred to as Alternative Business Structures (ABS) - jointly owned and managed by barristers and non-barristers such as other professionals or family members.

448. Both types of entity can operate as a traditional partnership, a limited liability partnership (LLP), or a limited company. The characteristics of these different entities are as follows:

Traditional partnership

- The partners are jointly and severally liable and thus there is no limited liability.
- There is no requirement to submit a copy of the partnership accounts to Companies House
- The partners are subject to income tax on their individual share of the total profits of the partnership.
- There is no tax advantage over the traditional self-employed barrister if the partnership is a barrister only entity.
- However, if the partnership is an ABS, there are potential advantages if for example a spouse with little or no earnings is given a partnership profit share.

Limited Liability Partnership

- The partners/members are protected by the limited liability nature of the entity.
- A copy of the partnership accounts has to be submitted to Companies House and must be in a format that complies with the Statutory Regulations.
- The tax treatment of an LLP is the same as that for a traditional partnership with the partners/members subject to income tax on their individual share of the LLP's total profits. So again, a barrister only LLP has no tax advantage over the traditional self-employed barrister.

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[51] See paragraph 3.1 of the Bar Council Ethics Committee "Entities" assistance document https://www.barcouncilethics.co.uk/documents/entities/

[52] See the Entites section of the BSB website for more information https://www.barstandardsboard.org.uk/for-barristers/bsb-entities.html

- But as with a traditional partnership, there are potential tax advantages where an LLP is an ABS with a spouse as a partner or member.

Limited company

- The directors/owners are protected by the limited liability nature of the entity.
- A limited company is taxed as a separate legal entity from the directors/owners.
- The company's profits are subject to corporation tax on its profits and the directors/owners are subject to income tax on funds extracted from the company in the form of dividends, salary payments or loan interest payments.
- Corporation tax rates are currently lower than income tax rates so a barrister-only limited company does allow the possibility of tax savings where some of the company's profits can be retained within the company and not drawn out by the directors/owners.
- And an ABS limited company with a low or non-earning spouse as a shareholder, allows the possibility of further tax savings even if all the company's profits have to be extracted as dividends or salary payments.

Taxation consequences of a self-employed barrister incorporating as a Limited company

449. A limited company is liable to corporation tax. The current corporation tax rate is 19% no matter the level of profits. However, in April 2023 this is due to increase to 25% for company profits exceeding £250,000, with a rate of between 19% and 25% for companies with profits between £50,000 and £250,000.

450. As the limited company and the director/shareholders are separate legal entities the profits within the company can generally only be withdrawn by the director/shareholders in the form of either salary or dividend payments. If the director/shareholder has made a loan to the company, funds can also with drawn as capital or interest payments. A salary is generally not tax efficient because of the employee and employer Class 1 National Insurance Contributions the company must be paid on the salary. So, paying the company profits out in the form of a dividend is generally preferred as dividends are not subject to National Insurance.

451. So, by incorporating and extracting income in the form of dividends, a barrister will make a saving of essentially the Class 4 National Insurance Contributions that would otherwise have been payable on self-employment profits.

452. A limited company registered as an ABS will permit a non-barrister to be a shareholder in the limited company. Where there is a non-earning spouse, that spouse could hold shares in the company and thus some of the dividends would be assessed

to income tax on that person and thus make use of their basic and potentially 40% rate tax bands.

453. If the barrister is in the fortunate position of not requiring all the income generated by the company, it would be possible to leave the income in the company to accumulate having only paid the lower rate of corporation tax. The owner can then draw dividends out at a later date when perhaps their income levels (and tax rates) are lower and thus obtain some tax advantage or at least a tax deferral.

Disadvantages and pitfalls of incorporation

- A limited company must prepare statutory accounts that comply with the Companies Acts. This means a balance sheet and detailed notes must be prepared as well as a profit and loss account.
- This inevitably will require a more detailed level of bookkeeping and higher annual accountancy costs to deal with the additional compliance work.
- A copy of the company's accounts must be filed with Companies House and these accounts will be in the public domain. However, the level of detail in these published accounts is much less than is required to be presented to the shareholders and HMRC. The accounts for Companies House are essentially a simple balance sheet. These accounts must be filed with Companies House within 9 months of the company's year-end.
- In the case of VAT, barristers enjoy the benefit of a special concession whereby VAT charged on fees is only payable to HMRC on receipt of payment of the fee. However, this concession will not apply to a limited company offering the services of a barrister. The consequence is that VAT is payable to HMRC on issue of a VAT invoice and thus at the end of a VAT quarter it is inevitable that VAT will be payable to HMRC on fees that have not been received by the company. This will clearly give rise to a cash flow disadvantage.
- There is available a cash basis for any business registered for VAT to adopt. The condition for using the general cash basis is that the business's turnover (fees) is less than £1,350,000. There is no application procedure; the business simply starts completing VAT returns on a cash received and paid basis. Once on the scheme the business must cease to use the cash basis when its turnover exceeds £1,600,000.
- Corporation tax is payable to HMRC 9 months and one day after the company's year-end. Whereas the deadline for submitting the corporation tax return to HMRC is 12 months after the company's year-end. However, the self-assessment tax return for the barrister is simpler in that there is no longer any requirement for the self-employment pages to be included.
- A Confirmation Statement must be submitted to Companies House each year confirming certain details including the names and addresses of the directors and the registered office. There is a small fee payable to Companies House for this return of, currently, £13.

- There are certain matters that will have to be dealt with differently, for example:
  - Motor expenses
    - A self-employed individual can claim a percentage of all motoring costs representing the business use of a car owned by the barrister.
    - With a limited company the company can own the car and then 100% of the costs become deductible from the income. BUT the director will be assessed to tax at their marginal rate on a benefit-in-kind. The benefit in kind is calculated by reference to a percentage of the list price of the car. The percentage applied depends on the CO2 emissions of the car measured in grams per kilometre and whether the car uses petrol or diesel. The current percentage varies from 1% for fully electric cars to 37% for cars producing more 170 g/km.
    - An alternative is for the director to own the car personally and to claim from the company a mileage allowance for business mile driven. The allowance that can be claimed without there being any tax consequences is 45p per mile for the first 10,000 miles and 25p per mile thereafter.
  - Pension contributions
    There is a potential problem with the barrister making personal pension contributions since, to claim tax relief, there must be earned income of an amount equal to the gross pension contribution, and dividend payments are not considered to be earned income. The solution is for the company to make employers' pension contributions on behalf of the director. These contributions will be deductible from the income of the company when calculating corporation tax.

Chambers

454. It may be necessary to amend the Chambers constitution to reflect the fact that some members of Chambers are practising through a limited company.

Summary

455. Clearly there could be tax and limited liability advantages to be gained by operating through a limited company. This is why incorporation has been a strategy that countless businesses have adopted for many years. However, there are complications and consequences that must be considered. Everyone is different and has individual circumstances have to be taken into account. It is essential that advice is taken from a suitably qualified accountant before taking any action. It is also essential that the regulatory implications are fully considered (see the Bar Council

Ethics Committee "Entities" assistance document[53] and the Entites section of the BSB website[54]).

[53] https://www.barcouncilethics.co.uk/documents/entities/

[54] https://www.barstandardsboard.org.uk/for-barristers/bsb-entities.html

Part Eleven: Making a Will

456. It is generally sensible to make a will and review it regularly. This should not only ensure that the estate passes to the right beneficiaries but also make administration of the deceased's affairs much simpler. This applies not only to barristers, of course, but also to their husbands, wives, civil partners, parents and adult children.

457. Without a will it is entirely possible that the operation of the rules of intestate succession will make things worse for surviving relatives than they need have been. Intestacy can cause many problems. It will often throw up a greater tax burden than need have arisen; it may create difficulties between a widow, widower or partner and the other beneficiaries; it may force a sale of the family home.

458. Although it is perfectly possible to produce a valid and effective home-made will, in all but the simplest cases it will be sensible to take advice from a solicitor (or other relevantly qualified professional) with whom all relevant matters can be discussed in detail, including all possibilities and the various fiscal considerations. This might include, for example, details of all life insurances or pension policies to ensure that these can be found promptly after death. A full and accessible statement (again regularly reviewed) of all assets and liabilities together with details of the locations of these, and the will itself, will assist enormously. It is also helpful to keep a list of internet account details and passwords.

459. Detailed advice on inheritance tax planning is outside the scope of this guidance but the following general points should be noted.

460. First, as the law now stands, any property left to a spouse or civil partner in trust for life or absolutely will be free of inheritance tax at that stage (except where the deceased is domiciled in the UK and the spouse or civil partner is not). There is also an exemption for gifts to charities.

461. Secondly, there is a "nil rate band" (£325,000 from 6 April 2009) meaning that gifts of property to this value do not attract Inheritance Tax (IHT) even if the relevant gift is not exempt. Taking these two points together, a person can leave £325,000 to children, for example, and the balance to a spouse or civil partner without there being any liability to inheritance tax. Until 9 October 2007, it was important to make use of this nil rate band. A straightforward way to do this was to leave an amount equal to the nil-rate band on discretionary trusts for family as a whole, so that it can be used to benefit children or widow(er)/ surviving civil partner as required (with the residue left to the spouse/civil partner). Otherwise, if the whole estate were left to the

spouse/civil partner, and was therefore exempt, the benefit of that nil rate band would be lost.

462. On 9 October 2007, however, the "transferable nil rate band" was introduced. This means that if a nil rate band is unused on the first death, the estate of the survivor benefits from an enhanced nil rate band. If the nil rate band was wholly unused on the first death, the nil rate band on the second death is doubled; if partly used, the increase is proportionate. This reduces the importance of the nil rate band discretionary trust, where property is otherwise to be left to the surviving spouse or civil partner (although there are still some situations in which it may be appropriate).

463. Although the nil rate band has not increased since April 2009, a further "residence nil rate band" has been introduced for deaths on or after 6 April 2017. This applies where individuals leave a residential property which has been their home to one or more direct descendant(s). The amount covered will initially be £100,000 (i.e. for 2017/18) on top of the nil rate band rising by £25,000 a year until it reaches £175,000 in 2020/21 (after which it will rise in line with the consumer prices index). The relief is "tapered away" at the rate of £1 for every £2 over £2m (so that there will be no relief for estates over £2.2m in 2017/18). There is also a "downsizing relief" available if a person has moved to a less valuable property since 8 July 2015 and leaves the smaller residence, or assets of equivalent value, to direct descendants.

Redirection of the estate

464. It is possible for a person's estate to be redirected within two years of death in such a way that inheritance tax is charged on the basis of the new disposition. In other words, the redirection is read back to death for inheritance tax purposes. This can be done either by the original beneficiaries (by "deed of variation") or, if the will is drafted to allow this, by the executors.

465. The second option can be very attractive to those who are not sure what they want done because they do not know what the circumstances will be when they die. But one or two things must be borne in mind before opting to create such a discretion. First of all, it places a burden on the executors; they must be clear as to what is expected of them, and they must be trusted to get things right. The provisions of such a proposed will must therefore be discussed with them first and their selection must be done with care, possibly consisting of one member of the family and one or two independent professionals who know the family circumstances. Secondly, if it is likely that the executors will give everything to the widow(er)/ surviving civil partner, this sort of arrangement may cause cashflow problems, because inheritance tax will have to be paid up front (on the grant of probate) and reclaimed when the estate is redirected and therefore becomes exempt. It will therefore be sensible to keep the

arrangements under review and if necessary execute a codicil (i.e. vary the will) as seems best from time to time.

Outstanding fees

466. It is worth noting HMRC's continuing acceptance that fees outstanding at death are not liable to inheritance tax. This practice is set out in the Inheritance Tax Manual[55]:

> *Outstanding barrister's fees or the fees due to a member of the Faculty of Advocates in Scotland do not form part of an estate. This is because they are deemed to be honoraria and, as such, are not recoverable by legal process. This applies even if the client has paid the fees into the hands of the instructing solicitor, Wells v Wells [1914] P157.*

467. It may therefore be sensible to consider leaving outstanding fees to children/grandchildren (or a family trust).

[55] See the inheritance tax manual at 10121 (April 2010).

Part Twelve: HMRC support

468. HMRC support is available for those having difficulty meeting their tax liabilities.

469. The Business Payment Support Service (BPSS) was introduced by the government to help self-employed people and businesses having difficulties in meeting their tax liabilities. It covers most taxes and duties including VAT, Corporation Tax, PAYE, National Insurance and Income Tax. Normally this will involve agreeing a "Time to Pay" arrangement which will allow payments to be spread over a number of months.

470. Further details are available from the HMRC website[56] or the dedicated telephone line on 0300 200 3835. If a payment plan is put in place before surcharges or penalties become due, these penalties will not apply, although interest will be charged.

[56] https://www.gov.uk/government/organisations/hm-revenue-customs/contact/business-payment-support-service

Annex 1 (Historic): Standard Rate VAT Increase - Bar Council Guide issued in 2011

This document is referred to in Part Six, paragraph 269. It was issued by the Bar Council to assist barristers and clerks when the rate of VAT was increased in 2011.

"1. On 4 January 2011 the standard rate of VAT will increase to 20%. This guide sets out key points of law of which barristers and their clerks will need to be aware. This is summarised at paragraph 16 below. It also responds to typical questions which the Bar Council has been asked, in order to show how the change will affect the administration of a barrister's practice.

2. HMRC has issued guidance ("VAT – Change of the Standard Rate to 20 per cent"). This covers barristers (and advocates) at section 9.2 as follows:

> ***9.2 Barristers and Advocates***
> *If you are a barrister or advocate and you follow the arrangements under which fee notes do not become VAT invoices until they are receipted, then the tax point for your fees is normally the date you receive payment. Fees received on or after 4 January 2011 will be liable to VAT at 20 per cent. If you receive fees on or after 4 January 2011 for cases completed before that date, you can declare VAT at 17.5 per cent... Similarly, if a fee received after 4 January 2011 includes services partly performed while the 17.5 per cent VAT rate applied, you can apportion your fees ...*
> This guidance is available online at http://www.hmrc.gov.uk/vat/forms-rates/rates/rate-rise-guidance.pdf .

Background

3. Although VAT on services generally becomes due at the earliest of (a) provision of the service (b) payment and (c) issuing of an invoice, there is a special rule for barristers. VAT on supplies made by barristers is chargeable at the earliest of the following times (see VAT (General) Regulations 1995, S.I. 2518, Regulation 92):

(a) when the fee for the barrister's services is actually received;

(b) when the barrister issues a VAT invoice;

(c) the day when the barrister ceases to practice.

4. Whichever of these dates applies to any set of circumstances is called the "tax point". It is crucial to note that the actual provision of services by a barrister is irrelevant when determining when a tax point crystallises.

5. It is also crucial to note that fee notes need not be, and those generated by standard software packages generally are not, VAT invoices[3]. Issuing a fee note does not, therefore,

create a tax point. Usually the tax point is the receipt of the fee (which is followed by the issue of a VAT invoice/receipt).

The change in rate

6. The rate of tax on a service is generally the rate in force at the tax point so (subject to the exception below) the VAT change which comes into effect from 4th January 2011 will have the following effects for barristers:

(a) If the tax point for a particular supply of services arises before 4th January 2011, the standard rate of VAT which must be charged is 17.5%;

(b) If the tax point for a particular supply of services arises on or after 4th January 2011, the standard rate of VAT which must be charged is 20%.

7. There is, however, a special rule that applies on a change of rate (VATA 1994 s 88(2) applied to reg 92 and therefore barristers by reg 95. See section 3.2 of the HMRC guidance). This applies where a service is provided *before* the change of rate but, under the special rules above, the tax point falls *after* the change of rate. The barrister may then elect for VAT to be applied at the original rate (i.e. at the rate in force when the work was done). There is no particular form of election required so simply issuing a VAT invoice showing the amount of VAT calculated at the relevant rate should suffice. In other words, a barrister who receives a fee on or after 4th January 2011 for work done before that date can choose whether to charge the rate that applies at the date of charge (20%) or the rate that applied at the date the work was done. The rates of VAT also changed on 1st December 2008 (from 17.5% to 15%) and 1st January 2010 (back up to 17.5%).

8. In practice, therefore:

(a) For work done on or after 4th January 2011, VAT must be charged at 20%.

(b) For work done between 1st January 2010 and 3rd January 2011, VAT can be charged at 17.5% (or 20 % if received on or after 4th January 2011).

(c) For work done between 1st December 2008 and 31st December 2009, VAT can be charged at 15% (or 17.5% if received before 4th January 2011, or 20% if received on or after 4th January 2011);

(d) For work done before 1st December 2008, VAT can be charged at 17.5% (or 20% if received on or after 4th January 2011).

9. From the barrister's point of view, there would be a slight cashflow advantage in charging the higher rate. It will generally be in the client's interests for the barrister to make the election to charge at the lower rate, however, either because the VAT is a real cost (because it is irrecoverable) or at least for cashflow reasons (because the VAT will have been paid out before it can be claimed as input tax).

Apportionment of fees

10. Where a supply of services spans the change of rate (i.e. some services are performed before and some after 4th January 2011), it is possible to apportion a fee received after 4th January 2011 so that so much of the fee as relates to work done before 4th January 2011 is charged at 17.5% (See section 3.4 of the HRMC guidance).

11. In practice, for ongoing matters, it may be simplest to issue fee notes in immediately before Christmas 2010 (or very early in January 2011), covering the work done to date with VAT shown at 17.5%. Even if the client does not pay immediately, the barrister and his clerk will have a contemporaneous record rather than having to perform the apportionment months or even years later. A separate fee note can be issued with VAT at 20% for all work done after on or after 4th January 2011.

Flat-rate scheme

12. The flat rate percentage will increase from 13% to 14.5% with effect from 4th January 2011.

13. Those using the flat-rate scheme will generally account for VAT quarterly and some will have a quarter that spans the rate change (e.g. one covering December 2010, January 2011 and February 2011). Such barristers should apply the 17.5% and 13% rates to receipts before 4th January 2011 and the 20% and 14.5% rates to receipts on or after 1st January 2010 (assuming they use the cash-based turnover method). In other words, those on the flat rate scheme (and using the cash-based turnover method) cannot elect to apply the rates in force at the time the work was done.

Pre-payments and anti-avoidance

14. In the normal course of things, barristers are paid after the work has been done, and issue VAT invoices after payment has been received. This means that the usual "tax point" for work done after 4th January 2011 will be the date of payment, and the rate of tax will be 20%. If, however, a barrister had been paid *before* 4th January 2011 for work to be done *after* that date, the rate of tax would be 17.5%. Similarly, if the barrister had issued a VAT invoice (not just a fee note) before 4th January 2011 for work to be done after that date, the rate would be 17.5% (although in this case the barrister might have to account for the VAT before receiving payment).

15. This result is subject to anti-avoidance rules introduced in Finance (No 2) Act 2010 (See Schedule 2. Detailed guidance on the legislation can be found at www.hmrc.gov.uk/vat/forms-rates/rates/anti-forestall-guidance.pdf). These apply in various situations including where:

(a) the barrister issues a VAT invoice that does not have to be paid in full within six months; or

(b) the payment or VAT invoice is in excess of £100,000, and this is not normal commercial practice.

16. At first glance, it might seem that these would apply to relatively few barristers. However, (a) since invoices are generally issued by barristers after receipt they will not generally show a date for payment and (b) it may be difficult to show that large pre-payments (let alone invoices) are normal commercial practice. A normal payment on account (i.e. one that would be made regardless of the change of rate) should not be caught.

Summary

17. In general, barristers can choose to charge and account for VAT at either the rate in force when the work was done or the rate in force when the fee is received. Assuming barristers will wish to charge the lowest rate (and ignoring prepayments and flat-rate scheme), this means:

(a) Work before 1st December 2008 can be charged with VAT at 17.5%;

(b) Work between 1st December 2008 and 1st January 2010 can be charged with VAT at 15%.

(c) Work done on or after 1st January 2010 and 3rd January 2011 can be charged with VAT at 17.5%.

(d) Work done on or after 4th January 2011 must be charged at 20%.

(e) Where work on a single matter spans a change in rate, the fee can be apportioned.

FAQs

Note 1: In these questions, it is assumed that "fee notes" are not VAT invoices.
Note 2: These questions are being asked on or after 4th January 2011 and relate to work done on or after 1st January 2010.

1. I am just about to send out a fee note for work done before 4th January 2011– what rate of VAT should I charge?

You can choose which rate to apply. The client will generally prefer the 17.5% rate (see paragraph 8).

2. Do I have to reissue fee notes for work done before 4th January 2011?

No, there is no need to reissue fee notes, although you could do so if convenient or on request.

3. I have just been paid for work I completed before 4th January 2011. The payment includes VAT at 17.5% as on the fee note. What rate of VAT should I include on the VAT invoice? Do I have to seek a payment of the 2.5%.

You should issue a VAT invoice showing VAT at 17.5% and account for that amount as VAT.

4. I have an ongoing case with some work before and some work after 4th January 2011. I have not yet been paid. Do I have to issue separate fee notes and/or invoices (some charging VAT at 17.5%, others at 20%)?

You are entitled to apportion the work between periods before and after 4th January 2011 and charge the different rates of VAT as appropriate but you do not have to issue separate fee notes. You could show difference rates on the same fee note (and invoice).

5. I am being paid in instalments for an ongoing case. The first instalments have been billed and paid with VAT at 17.5%. The most recent fee note sent out showed VAT at 17.5%. Do I need to reissue the fee notes? Or is it OK to switch to 20% for future fee notes only?

Provided the most recent note relates to work done before 4th January 2011, you do not need to reissue the fee notes but should switch to 20% for future fee notes (but only if they relate to work done after 4th January 2011)."

Annex 2 (Historic): Computation of Profits for Income Tax Purposes: Application of UITF 40 to Barristers' earnings – Bar Council Guide issued in 2005

This historic document was issued by the Bar Council in 2005. It relates to the subject matter in paragraph 43 of Handbook. Barristers occasionally ask the Bar Council for a copy of the document and the 1999 Guidance note that it referred to. It is included on that basis. Part 1 of the Handbook should however be used as providing the more up-to-date guidance.

"1. The Bar Council has been asked to provide guidance on the application of Urgent Issues Task Force Abstract 40 ('UITF 40') to the computation of barristers' earnings. This Note updates the guidance given in the Guidance Note of 10 March 1999 ("the 1999 Guidance") provided in Annex 1.

2. These changes do not affect barristers in their first seven years of practice, who may continue to use a cash basis for tax purposes.

3. UITF 40 was issued on 10 March 2005 in response to questions that had arisen following an amendment (Application Note G) to Financial Reporting Standard 5 ("FRS 5"). It applies to accounting periods ending on or after 22 June 2005 and is concerned with the recognition of revenue for accounting purposes in the case of service providers. Although most likely to affect large professional firms of e.g. solicitors and accountants, it is in principle relevant to barristers as well.

4. Two principles govern the application of UITF 40 in relation to FRS 5:

a. Contract activity rather than contract completion or invoicing is the focus of revenue recognition; and

b. When work is partly performed at the end of the barrister's accounting period, the fair value of the right to consideration should be brought in as revenue.

5. Our view is that this affects paragraphs 6 and 7 of the 1999 Guidance, and that a barrister can no longer ignore all 'work-in-progress' regardless of the circumstances.

6. If in any particular case or matter, work has been performed by the end of the accounting period for which a barrister has 'obtained a right to consideration', then for accounting periods ending on or after 22 June 2005 that work should be taken into account in the same way and to the same extent as 'completed work' as explained in paragraphs 9 to 12 of the 1999 Guidance.

7. We believe that it will be rare indeed for UITF 40 to require adjustments for any individual barrister in relation to more than a handful of cases or matters, and it may well be that in many cases the 'materiality concept' – as explained by the Inland Revenue in the 1998

Press Release reproduced at paragraph 4 of the 1999 Guidance – will come into play, with the result that it would be inappropriate and unnecessary for many barristers when applying the 1999 Guidance to make any further UITF 40 adjustment to their computation of profits for tax purposes.
8. Certain typical payment scenarios (taken from the guidance issued by the Institute of Chartered Accountants in England and Wales (the "ICAEW Guidance") are attached to this note, with accounting comment.

9. To sum up:

a. Work completed at the end of the barrister's accounting period must be brought into account as debtors, in the amount of the agreed or anticipated fee.

b. In the case of incomplete work that straddles the end of the barrister's accounting period, it is necessary to bring in a reasonable estimate of the fee earned as a result of the work done at that date.

c. All the above is subject to the "materiality concept" referred to in paragraphs 4 to 6 of the 1999 Guidance.

10. When income accrued under UITF 40, which has not previously been recognised, is first brought into charge, Finance Bill 2006, cl 102, Sch 15 provides that three years' spreading relief will be available in respect of the 'adjustment income' (or up to six years if the adjustment income is more than one-sixth of the profits of the business for any of the first three years following the change).

11. The adjustment does not count as profit for NIC purposes, but is pensionable.

Example

A barrister draws up accounts for the calendar year.

His profits for the year ended 31 December 2004 were £10,000 (ignoring UITF 40) and £11,000 (applying UITF 40).

Accordingly the previous year adjustment is £1,000.

His profits for the year ended 31 December 2005 are £18,000 (applying UITF 40).

To this must be added the adjustment to opening debtors (£1,000) but this maybe spread over three years, i.e. £333 per year.

So his profits for 2005/2006 are £18,000 + 333 = 18,333.

Common Fee Payment Scenarios

Q1 - Barrister- "no win, no fee"

A barrister works on a "no win, no fee" basis. How should this be accounted for?

Revenue should not be recognised until a case has been won. Only at that stage does the barrister have a right to consideration. (UITF 40, para 27)

Q2 - Barrister- "pay at end"

A barrister works on a "pay at end" basis. The fee is not agreed in advance, nor will the rate be fixed. The consideration is negotiated at the conclusion of the case. The difference from 'no win, no fee' is that a fee will always be due. Currently this is included as soon as the fee is negotiated.

There is significant uncertainty about the amount of the fee at an accounting date prior to the end of the case. Nevertheless, it is clear that the relevant fee is not nil.
There are two possible arguments:

- Where there is some uncertainty about the fee but a reasonable estimate can be made, at least of the minimum that will be earned, then an estimate should be made of the part of the total fee that has been earned as a result of work done to the balance sheet date. This estimated amount should be included as revenue.
- Where there is genuinely so much uncertainty that no reliable estimate can be made of the total fee and of the part of that total that has been earned to date, no revenue should be recognised until such time as the uncertainty has reduced and a reliable estimate can be made. This might be at a later stage of the case or it might not be until the fee is negotiated at the end of the case, depending on the facts and circumstances. There is a general assumption that amounts can be estimated with sufficient reliability to be included in financial statements. Non-recognition due to an amount not being reliably estimable should be very much the exception.

Q3 - Barrister- fixed fee cases

A barrister works on certain types of public funded cases ("cost assessed", "graduated fee" and "prosecution"). These cases are done for a fixed fee. Currently, revenue is recognised on completion of the case. Is it right to say that UITF 40 can be read to give the same result? Another view appears to be that every case should be examined and part of the consideration accrued to the year-end date be included, even though there is no right to consideration. A further reason why one might argue that this is incorrect is that if the barrister who has prepared the case is unable to present the case in court then the presenting barrister receives the whole of the fee.

The appropriate accounting here is a matter of professional judgement depending on the facts of the situation. Where, for example, it is reasonably clear what a typical case involves (say two client meetings, one day's preparation and one day in court for an aggregate fee of £5,000), it will be possible to assess, for each case, how far through the case one is at the year end. If the barrister is halfway through the case, he would recognise half the fee, or perhaps somewhat less if there were genuine uncertainties about the time to complete. On the other hand, if the fee was agreed but the amount of remaining work and therefore time was open ended and therefore very difficult to

predict, one would either (a) recognise some revenue but on the basis of a very conservative estimate or (b) argue that no reliable estimate can be made until the case is further progressed.

As to the point about potentially losing the fee if the barrister cannot appear in court, the effect of this point on the accounting depends on the substance. If losing the fee due to being unable to present the case in court is rare, one would either disregard it or make an overall reduction of a few percentage points in the overall revenue figure to allow for the rare case in that category. On the other hand, if it is common that a barrister prepares a case and is not able to present it, thereby losing the fee, it may be that there is not sufficient certainty to justify recognition of revenue until the barrister does present the case in court and is thereby assured of earning the fee. Events after the balance sheet date (appearing or not being able to appear) may of course reduce the uncertainty in some cases.

Q4 - Barrister- Legal aid cases

Legal aid in some cases is not agreed until after the matter has been settled. In lengthy cases payments on accounts are made. This is a long and protracted procedure that can take many years. Often the payments on account will be for a greater amount than the eventually agreed fee and the barrister has to return the excess. It has been agreed with HMRC that the relevant tax point is payment, normally a payment on account, or the agreement of the fee, whichever comes first.

Again, professional judgement has to be applied here and the accounting treatment will depend on the degree of uncertainty. In principle, revenue should be recognised according to the work done to date, rather than according to progress payments received. If a reasonable estimate can be made of the revenue that has been earned as a result of the work done to date, then that should be recognised. Prudence should be built in to that estimate in response to uncertainty. It may be that the level of uncertainty is so high that no reliable estimate can be made until either later in the process or until the case is completed and the fee agreed. Finally, a barrister should not recognise all the progress payments received as revenue, even if they do bear a close relationship to the work done to date, if it is likely that some of the amounts received will have to be refunded.

COMPUTATION OF PROFIT FOR INCOME TAX PURPOSES OF BARRISTERS BAR COUNCIL GUIDANCE NOTE on the application of FA 1998, Section 42: agreed by Inland Revenue

Introduction

1. Section 42 of the Finance Act 1998 requires all professionals (except barristers and advocates in their first seven years of practice: see paragraph 18 below) to compute their profits for income tax purposes on "*an accounting basis which gives a true and fair view*" of those profits. This note, the contents of which have been agreed with the Inland Revenue, seeks to set out

how the new provision will apply in practice to barristers in England and Wales, to give particular guidance as to the adjustments necessary to convert a "*cash basis*" profit to a "*true and fair*" one, and to answer some of the questions most likely to arise.

General Principles: "*True and fair view*"

2. The phrase "*true and fair view*" is borrowed from what is now Section 226 of the Companies Act 1985 which provides inter alia that every company must prepare a profit and loss account which must "*give a true and fair view of the profit or loss of the company for the financial year*", and consistent legal advice on that and earlier legislation has been that although the question whether accounts satisfy the "*true and fair*" requirement is ultimately a question of law for the Courts, that question cannot be answered by the Courts without evidence as to the practices and views of accountants, especially as set out in accounting standards developed by the Accounting Standards Board or its predecessor body and published as Financial Reporting Standards (FRSs) or Statements of Standard Accounting Practice (SSAPs).

3. Although there is no FRS or SSAP in existence which lays down accounting standards for arriving at a "*true and fair view*" of the profit of a barrister for a period of account, the opinion of accountants confirms that Although there is no FRS or SSAP in existence which lays down accounting standards for arriving at a "true and fair view" of the profit of a barrister for a period of account, the opinion of accountants confirms that computing profits on the old "*cash basis*" (which takes no account at all, either of fees earned but not received, or of expenses incurred but not paid, during the year) does not give a "*true and fair view*" of his or her profit for that year, because of the possibility (indeed in many cases, probability) of distortion. Accounting principles require at least some account to be taken of fees earned and expenses incurred during the year, but this is subject to the materiality principle and the prudence principle discussed below.

4. The 1998 Budget Day Press Release issued by the Inland Revenue says, under the heading "*Use of 'true and fair view'*":

> "24. *The aim of the proposals is to apply the earnings basis to professionals ... The earnings basis is already the basis which applies under the existing law to some professionals and to traders. We believe that the accountancy concept of a "true and fair view" does the job in a concise yet flexible way because:*
>
> 1. *accounting standards as they currently operate are applied and so the tax treatment can adapt automatically to changes in those standards; and*
>
> 2. *the accountancy concept of 'materiality' is imported, which means a practical view can be taken of the time when immaterial amounts are recognised.*
>
> 25. *The materiality concept is particularly relevant in arriving at work-in-progress. It permits a broad-brush approach in small cases or for small amounts. Although there may be occasions where accountancy practice is displaced by a rule of tax law, the Inland Revenue do not consider such an approach to materiality in the*

valuation of work-in-progress, if sanctioned by accountancy practice, to be inconsistent with tax law.

26. The 'true and fair view' approach is concerned only with the computation of taxable profits or losses. For these proposals it: ...

2. does not require accounts to be drawn up on any particular basis; for example, cash basis accounts could still be prepared provided adjustments are made to convert the profit to an earnings basis profit in the tax computations;

3. does not require accounts to be audited;

4. does not require additional disclosure or require a true and fair view balance sheet to be prepared."

5. It is assumed that barristers will continue to prepare accounts on a cash basis, and make annual adjustments to convert the profit to a "*true and fair*" profit for tax purposes. In theory, adjustments need to be made both to the receipts side of the account and to the expenses side. However accountancy principles, including the materiality concept mentioned above, do not require the adjustments to be as complex as might be thought. The annual adjustments required are explained below.

No adjustment for work-in-progress

6. Accountancy principles normally require work-in-progress to be brought into account (or "*recognised*") at the lower of cost or net realisable value. It is accepted that a professional's time costs him or her nothing, and so since barristers do not normally have any fee-earning employees (whose salaries are the main component of work-in-progress in, say, a solicitors' firm), the cost to them of their work-in-progress would normally be confined to direct overheads, such as transport, and indirect overheads such as a proportion of the cost of heat and light of their chambers or other accommodation. In view of the materiality concept these overhead costs may be ignored on the broad-brush approach, so that barristers need not normally make any adjustment for work-in-progress at all.

What is work-in-progress?

7.1 In view of paragraph 6 above, it is of course necessary to define what is meant by "*work-in-progress*". Essentially, this is "*work not yet completed at the accounting date*", and "*work*" will normally be "*completed*" when the case or matter in respect of which the barrister has been instructed is concluded.

7.2 So, for example, the work of a barrister in respect of a particular matter will normally be completed in the following circumstances, namely (a) in a criminal case, when sentence has been passed, or the defendant discharged upon acquittal; (b) in a civil case, when the court has delivered final judgment and awarded costs; and (c) in purely advisory work, when it is agreed between the barrister and the client that the work is at an end. These are of course the simplest of examples, and the Institute of Barristers Clerks is going to discuss more detailed guidance with the Inland Revenue. For work to be "work-in-progress" rather than "completed

work" the barrister needs to be satisfied that the matter is still continuing. Normally the Revenue would not seek to disturb the barrister's judgement but it can question decisions if they seem to be unreasonable. Any disagreement would be for the usual tax appeal procedures to resolve.

7.3 Note that if the barrister is briefed to appear in, say, the High Court, the possibility or indeed probability that he or she will subsequently be briefed again in the same matter (e.g. on appeal to the Court of Appeal) will not normally affect the time when the work on the original brief is "*complete*"; any further brief should be treated as a separate piece of work which will in turn be complete when the Court of Appeal has delivered final judgment and awarded costs. However if there is a specific agreement that the client will not pay the fee until a specified stage of the case or until the case is finally over - as is the situation in several categories of cases e.g. personal injury (especially involving trade unions and insurance companies), medical negligence, payments out of trust funds - then the work is to be regarded as "incomplete" until the stipulated stage is reached or the case is finally over. However once work is completed, anticipated delay in payment would not normally be relevant to the question whether work is or is not "*complete*" (for the relevance of delay in assessing whether receipt is "*reasonably certain*", see paragraph 12 below).On the other hand, if the fee is <u>conditional</u> upon a particular outcome, then nothing needs to be brought into the accounts unless and until that outcome has been achieved; for until then it is not "*reasonably certain*" that the fee will be received.

<u>Adjustment for work not completed but for which interim payments received</u>

8. Normally, if it is agreed that payments on account are to be received whilst a case is still going on, there is no question of those payments having to be repaid by the barrister, and in such circumstances, no adjustment is appropriate. However in certain cases (interim payments in some legal aid cases, in particular) there is a material risk of all or part of the payments having to be returned. In such cases, it follows from the status of the case as "*work-in-progress*" that, to the extent that there is in any case a material risk that an interim payment may have to be returned, then to that extent such interim payments should be <u>excluded</u> from the '*true and fair*' profit for the year, and brought back in only when the work is "*complete*"

<u>Adjustment for completed work for which fees not received</u>

9. Having identified work which is "*completed*" but for which payment has not been received as at the end of the period of account, the next task is to compute the "*value*" of that work. Accounting principles require one to bring in such work at the amount of the fee, if any, which is "*reasonably certain*" to be received.

10. In a case where the fee has been agreed (or is otherwise known) in advance, or although not agreed in advance, has been agreed, "*taxed*" or otherwise assessed by the time the barrister's accounts are being finalised (see para.15 below) there will not normally be any difficulty: unless there is some particular reason to suppose that the fee will <u>never</u> be paid (equivalent to a '*bad debt*'), or that the client is going to insist on renegotiating the fee downwards, the "*value*" of the completed work is the agreed fee. Note that in a case where the fee has been subject to "*taxation*", but the barrister is still appealing (and thus hoping for

an increase), the "*taxed*" figure should be brought in to the adjustment as being "*reasonably certain*", and any increase will fall into a subsequent year.

11.1 In a case where the fee is not agreed or otherwise known at the time the accounts are being finalised (e.g. where it is still subject to "*taxation*" or other assessment by the Courts), then standard accountancy principles (in particular, the "*prudence*" principle) only require so much as is "*reasonably certain*" to be paid to be brought in. In many cases this may be a difficult exercise, but in relation to most matters it ought to be possible for the barrister (and/or the clerk) to arrive at a minimum figure, which could be brought in to the adjustment. However, it is not essential for accountancy purposes that this estimate be done on a case-by-case basis. It is entirely acceptable for barristers and their clerks to take a "broad brush" approach to a basketful of similar-sized cases. If for example a barrister has 200 small cases (for which the fees have not yet been "taxed" or otherwise agreed) outstanding at the time the accounts are being finalised, for which the total fees applied for are say £40,000, and from experience his or her clerk reckons to get between 40% and 70% of the fees applied for overall, then they should be "reasonably certain" of receiving 40% of £40,000 = £16,000 for that basketful of cases, and should therefore bring £16,000 into the end-of-year adjustment. "Small" would vary from barrister to barrister; £1000 might be an appropriate cut off figure for many. Larger cases could be dealt with either on a case-by-case basis, or put into another "basket" provided they were of similar size so that one did not distort all the others. If in any particular case or group of cases it is not possible to be reasonably certain that any amount will be received, then nothing need be brought in until and to the extent that some amount is reasonably certain to be received.

11.2 In relation to legally-aided work, the fee for which is still awaiting "taxation" or other assessment at the time the accounts are being finalised, the position is even more "up in the air" as indeed has been illustrated by the recent (June 1998) House of Lords hearing. In some cases, work is done on a graduated fee basis which permits a reasonable estimate to be made of the minimum fees due. Where this is the case, that minimum amount should be included. In other cases it may genuinely not be practicable for the barrister to make a reasonable estimate of his or her entitlement to a fee nor of the tax year in which he or she is likely to be paid anything. Accountancy advice received indicates that the element of guesswork involved in arriving at any "reasonably certain" figure in these cases is such that in all the circumstances (which include the fact that in many cases there is a delay of several years in getting the fee "taxed", let alone paid) it would be a reasonable accounting practice on grounds of prudence to leave such legally aided fees out of account until the year in which they are "taxed" or otherwise assessed. Accounts consistently prepared on that basis would be "true and fair". The prudence principle and the practical considerations of certainty and objective verification justify this approach to legally aided fees.

The relevance of delay in assessing "reasonable certainty"

12. The application of the materiality principle as explained in paragraph 11 above should cut out problems concerned with the worst cause of delay (delay in "*taxation*"). Mere anticipation of delay in payment of an agreed fee would not, on the other hand, of itself prevent it being recognised for accounting purposes. But in many cases, the fact that there has been a severe delay in the payment of a fee will suggest that there is a doubt as to whether it will be paid at all; if this is, on enquiry, confirmed to be the case, (so that the debt can be classified as bad or

doubtful) it would justify making a provision (i.e. a deduction) in respect of some or all of the amount; further, if a fee has been outstanding for more than 2 years since the submission of the fee note (in which circumstances it will no longer qualify for recovery under the Bar Council's current machinery for fee collection) then it may be assumed that it will not be paid unless there is some positive reason to suppose that it will.

Adjustment for expenses incurred but not paid

13. In computing profits on the cash basis, account is only taken of expenses actually paid in the year, and expenses incurred but not paid during the year are ignored. On a "*true and fair*" basis, an adjustment is necessary to deduct from profits any material expenses incurred but not paid during the year. For example, if a barrister is liable to pay clerk's commission as a percentage of his or her fees, then the barrister may treat as an expense incurred but not yet paid the clerk's commission which will in due course have to be paid on the fees brought into account in the annual adjustment as earned but not yet received.

How to make the annual adjustment

14.1 This adjustment only has to be carried out once a year. It is not necessary to keep running records throughout the progress of a case, or change computer programmes, or incur material extra bookkeeping or accountancy costs. All that a barrister (in conjunction probably with his or her clerk) has to do is arrive at figures for "*fees for completed work reasonably certain to be received*" and "*expenses incurred but not yet paid*" as at the end of each year of account.

14.2 To convert profits computed on the cash basis into profits on the new "*true and fair*" basis, the following exercise is all that is required:

	£
Profits on cash basis for year ended (say) 30th April 2001	xxx
Adjustment as at 30th April 2001 ("the closing adjustment")	
Add fees for completed work not received as at 30th April 2001 net of any provision for bad debts thereon	+xxx
Deduct any interim payments received on W-I-P as at 30th April 2001 which need to be excluded in accordance with paragraph 8	-xxx
Deduct any expenses incurred but not yet paid as at 30th April 2000	-xxx
Add any expenses paid on or before 30th April 2001 which relate to years after 30th April 2001	
Add any expenses paid on or before 30th April 2001 which relate to years after 30th April 2001	+xxx

<u>Adjustment as at 30th April 2000</u> ("the opening adjustment")		
Deduct fees for completed work not received as at 30th April 2000		-xxx
Add any interim payments received on W-I-P as at 30th April 2000 which need to be excluded in accordance with paragraph 8		+xxx
Add expenses incurred but not yet paid as at 30th April 2000		+xxx
Deduct any expenses paid on or before 30th April 2000 which relate to years after 30th April 2000		-xxx
Profit on "*true and fair*" basis for year ended 30th April 2001	=	xxx

14.3 In most cases there will be no need to deduct interim payments as there will be no risk of their having to be returned. In cases where such a material risk exists, the deduction may be made (see paragraph 8 above).

14.4 One-tenth or more of the catch up adjustment (see paragraphs 16 and 17) falls to be added to the figure of true and fair profit.

14.5 The following example may be helpful:

- Barbara Barrister prepares her accounts to 30 April each year and for her own purposes continues to prepare them on a cash basis. She draws up her accounts to 30 April 2001 some time in November 2001. So she first draws up accounts to 30 April 2001 on a cash basis, giving a figure of profits of (say) £25,000. These "cash basis" profits then need to be adjusted to give a figure of "true and fair view" profits for tax purposes.

- Barbara needs to identify work which is "completed" at 30 April 2001 but for which payment has not yet been received and to estimate the amount of fees which she is reasonably certain (on the basis of the information available to her at November 2001) to recover for that work. She will do this in accordance with paragraphs 9-11 of this Note. Some of these fees might have been paid by November 2001 but some might not. Suppose this amount "owed" to her totals £15,000.

- Next she may have received some interim payments in the year to 30 April 2001 in circumstances where there is a real risk that they might have to be returned (or they might even have already been returned by November). Suppose these total £3,000.

- Next she might have incurred expenses relating to the year to 30 April 2001 which she had not paid at 30 April 2001, for example, Chambers expenses or Clerk's fees. Suppose she estimated the total of these as £2,500.

- Next she might have "bad debts", that is, amounts which were brought into her tax profits for earlier years which she now thinks she is unlikely to receive. Suppose these total £1,300.

- Finally she paid annual rent on a leased car in advance of £2,400 on 1 January 2001, so £1,600 of this relates not to the year ended 30 April 2001 but to the following year.

- All this gives a **closing adjustment** of £15,000 - £3,000 - £2,500 - £1,300 + £1,600 = £9,800.

- Barbara also needs to make an **opening adjustment** to reflect the state of affairs at 1 May 2000. This will be made using the same principles as the closing adjustment for the **previous** year. Assume this was, say, £8,000.

- So her profits for tax purposes are £25,000 + £9,800 - £8,000 = £26,800 (to which the catch up adjustment falls to be added: see paragraph 17.4).

When to make annual adjustment

15. The computation of the annual adjustment does not have to be carried out on the last day of the barrister's accounting period - in practice, it need only be carried out when the accounts for an accounting period are being finalised for the purpose of completing the relevant tax return. If, as in the above example, the accounting period runs to 30th April, then the tax return for the year ended say 5th April 2002 will include the profits for the period of account ended 30th April 2001. That tax return is due in to the Inland Revenue by 30th September 2002 (if you want the Revenue to compute your tax liability) or 31st January 2003 (if you are going to compute your tax liability yourself). Accounting principles allow (indeed require) accounts to reflect the commercial position at the time they are finalised, even though this is some time after the end of the period of account. Therefore, for example, a fee for completed work which was uncertain in amount at the end of the period of account (say at 30th April 2001) but which had been agreed or even paid by the time the accounts were finalised (say November 2001) would be brought in at the agreed or paid figure; conversely, a fee which had been agreed and was apparently "*good*" at the end of the period of account, but which was known or thought to be "*bad*" by the time the accounts were finalised, would be made the subject of a bad debt provision.

The "*catch up*" charge

16.1 Section 44 of, and Schedule 6 to, the Finance Act 1998 provide for a "*catch up charge*" on switching from the cash basis to the "*true and fair*" basis. The purpose is to bring into charge to tax the adjusting figure which would otherwise fall out of charge between the last year of computing profits on the cash basis and the first year of computing profits on the "*true and fair*" basis.

16.2 The "*catch up adjustment*" is computed in exactly the same way, and on the same principles, as the "*closing adjustment*" described at paragraph 14.4 above.

16.3 For those not affected by Section 43 "*Barristers and Advocates in Early Years of Practice*" (as to whom see paragraph 18 below), the "*catch up adjustment*" will be calculated as at the last

day of the period of account which falls in the fiscal year 1999/2000, the last period for which profits may be computed on the cash basis. This will be the period that ends between 6th April 1999 and 5th April 2000 (inclusive), because *the "true and fair"* basis applies for periods of account beginning after 6th April 1999. So for a barrister making up accounts to 30th April, the last year for which the cash basis may be used is the year ended 30th April 1999; the "*catch up adjustment*" will be computed as at 30th April 1999; the period of account 1st May 1999 to 30th April 2000 will be the first period for which profits must be computed on a "*true and fair*" basis; and the "*catch up adjustment*" as at 30th April 1999 will form the opening adjustment in converting the profits for the year ended 30th April 2000 from the cash basis to the "*true and fair*" basis.

16.4 Consider again the facts in the case of Barbara Barrister set out in paragraph 14.4 above. Suppose the facts were the same except that they related to the year ended 30 April 1999. So all the references to 30 April 2001 become references to 30 April 1999. Similarly, references to 30 April 2000 become references to 30 April 1998.

16.5 The year ended 30 April 1999 is Barbara's last year on the cash basis and it forms the basis for her 1999-2000 tax liability. She is taxable for that period on her cash basis profit of £25,000. In addition, her catch up adjustment is the "closing adjustment" amount of £9,800. There is no "opening adjustment". This is because the opening adjustment removes amounts which were brought into tax in the previous year on the "*true and fair*" basis. Since this is the last year on the cash basis those amounts will not have been brought into tax in the previous year.

17.1 The "*catch up adjustment*" is brought into charge to tax by being added to a barrister's profits over a period of up to 10 years. In the absence of any election, one-tenth of the "*catch up adjustment*" will be added to profits in each of the first 10 periods of account for which the profits are calculated on the new "*true and fair*" basis; this is subject to a "*capping*" provision which limits the figure added to profits in any of the first 9 periods of account to 10% of the profits for that period; where the capping provision has applied in any year, the balance is added to profits in the tenth year. Generally the *"catch up adjustment"* will be brought into charge in the ten fiscal years 1999/2000 to 2008-09; however, where a barrister draws up accounts to 5th April 2000, and does not draw up any other accounts to any other date in the fiscal year 1999-2000, the *"catch up adjustment"* will be charged to tax in the ten fiscal years 2000-01 to 2009-10.

17.2 However, during the spreading period, a barrister may elect to pay tax on more of the adjustment for any year than would otherwise be charged. This may be beneficial, for example, if he or she has losses from other sources for that year.

17.3 These spreading provisions are intended to mitigate the cash flow effect of requiring barristers (and other professionals) to change to a "*true and fair view*" basis.

17.4 In paragraph 16.5 we saw that Barbara Barrister's catch up adjustment was £9,800. Subject to the "*capping*" rule and to her option to make payments earlier, this amount will be taxable in ten equal instalments under Case VI of Schedule D. That is, £980 will be taxable income for each of the ten tax years 1999-2000 to 2008-2009.

Barristers in Early Years of Practice

18. Section 43 of the Finance Act 1998 provides that barristers may compute their profits for tax purposes on a cash basis for periods of account ending not more than 7 years after they first commence in practice.

At the end of 7 years (or earlier if they choose) barristers must move to a "*true and fair*" basis complying with Section 42. Although at that point there will be a "*catch up*" adjustment charge, this charge will be subject to the same spreading and capping provisions (over the 10 years from the date of change) as explained above in relation to established barristers."