

# The Office of Tax Simplification: Looking Back and Looking Forward



TLRC  
Discussion  
Paper No. 11

Tracey Bowler  
**Tax Law Review  
Committee**

**The Office of Tax Simplification:  
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*Tax Law Review Committee*

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\*See footnote 1

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## **1 Introduction**

- 1.1 The Office of Tax Simplification (OTS) was set up by the current government more than four years ago. With less than one year left of its initial fixed term, this discussion paper considers what the OTS has achieved to date and what can be learnt about the impact of the OTS on simplification of the tax system. It considers what conclusions can be drawn from the past four years in assessing whether the next government should continue with the OTS and what changes to its operation could be considered.
- 1.2 The paper is written for the Tax Law Review Committee (TLRC) of the Institute for Fiscal Studies.<sup>1</sup>

## **2 Executive summary**

- 2.1 Simplification of tax matters will never be easy and the UK tax system is unlikely ever to be simple. The world in which the tax system operates is too complex and there will always be political and economic reasons that take precedence over a simplification agenda. That said, considering the OTS's limited resources, it has been productive. Its consultative approach speaking to a wide range of taxpayers, advisers and HM Revenue & Customs (HMRC) front-line staff across the country is to be warmly welcomed. Overall, the UK tax system has benefited from the work of the OTS. Changes made over the last four years may still leave much left to do, but those changes almost certainly would not have occurred without the OTS.
- 2.2 The OTS can be a significant driver of changes and has the potential to be an internal force for policy decisions to take into account simplification issues. It can offer considerable expertise, based not only on technical knowledge but also on the breadth of consultation it engages in. Although there are arguments for the OTS to have more independence, the value in its collaborative working with HMRC and HM Treasury leads to the conclusion that added independence would not be beneficial overall. However, the OTS should be put onto a more permanent footing. Its work on simplification transcends the cycle of government.
- 2.3 Looking at the work the OTS has done in the last four years, it is clear that both administrative and substantive changes are needed to simplify the UK's tax system. However, the response or lack of response by government to many of the substantive changes recommended by the OTS has left an impression that the OTS is focused on administrative changes and that there is insufficient appetite in government for more radical changes to simplify the system. At

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<sup>1</sup>John Whiting, Tax Director of the OTS, is a member of the TLRC but has played no part in the preparation of this paper apart from answering the TLRC's questions on the work of the OTS and checking some aspects of the draft paper for factual accuracy.



times, administrative recommendations have also been dismissed by government with too little explanation.

- 2.4 Serious problems have arisen on implementation of some of the OTS's proposals. This was perhaps most marked in the case of the changes to small businesses' tax calculations. Implementation suffers from a lack of OTS involvement. For example, in the case of the small business changes, the limits and basic assumptions for the changes set out by the OTS seem to have been ignored.
- 2.5 The limitation on the OTS considering only existing law and not any changes proposed during a project suggests that the OTS is not at the heart of the tax-policy-making process. There have been various instances of the OTS making particular recommendations and at the same time changes being introduced, which at worst expressly contradict the recommendations without explanation and at best suggest a dismissive or limited view of the OTS's work. While policy decisions are a matter for Parliament, the OTS could offer advice and improve consistency of approach. There will be times when other considerations, especially political, take precedence over the simplification objective, but a fuller explanation of divergence from OTS proposals would mean that at least the OTS's work would appear to have been considered. Simplification needs to become embedded in the policy-making process and not seen as stand-alone or as an afterthought.
- 2.6 It is of concern to see the OTS prevented from considering issues that it has considered before and where proposals were rejected by government. It may be that the same recommendation will be made with the same response, but recommendations can change and so can the response of government. Consideration of all relevant issues is key to keeping the respect of the tax community.
- 2.7 To make a greater impact on simplifying UK tax law, the standing of the OTS's recommendations needs to increase. It may be that government chooses not to follow recommendations, but an explanation of why not would show greater support and recognition of the OTS's work. The pressure to produce 'quick wins' and to fall in with the Autumn Statement and Budget timetables (which already cause problems for the system themselves) should be resisted.
- 2.8 When the OTS was first proposed by the then Opposition, it was to report to a new Joint Parliamentary Committee on Taxation. An advantage of such a committee would be that, to an extent, it could be the driver of the simplification process. The added level of scrutiny of response to recommendations could be beneficial. In addition, the Committee could hold HMRC and HM Treasury to account for the response to the OTS's reports. Both HMRC and HM Treasury are organisations with significant pressure on

their resources. It would not be surprising if their preference were for maintaining the status quo rather than pushing forward significant change. The Committee would have the potential to overcome that force of inertia, although it would still need to be recognised that Ministers have the final say on what measures are put to Parliament for implementation.

- 2.9 The resources of the OTS have been minimal over the past four years. A significant increase in resources is needed to enable it to promote more significant simplification.

### **3 Background**

- 3.1 In 2005, the Conservative Party's Working Party on tax reform chaired by Lord Howe set out a plan for tax reform and simplification.<sup>2</sup> In particular, it proposed the formation of an Office of Tax Simplification.<sup>3</sup> The OTS would operate in a similar way to the National Audit Office, reporting to a new Joint Parliamentary Select Committee on Taxation and would be overseen by a Steering Committee appointed by the Chancellor of the Exchequer. It would be set up to be an independent and authoritative voice on tax law with parliamentary backing to 'establish and institutionalise ... a process, whose continuing insistence on simplicity is as irremovable, and as constantly present, as the voice of the tax-raising departments – and as the politically restless, impatient input of successive Chancellors'.<sup>4</sup> As well as staff from HMRC and academia, the OTS would include individuals from the tax professions to provide expertise and a fresh perspective. In addition to its role in reviewing existing tax law, the OTS would examine proposed new legislation, to determine whether it was consistent with the principles of sound tax law and was reasonably simple. However, it was recognised that, in the early years at least, the review of new legislation might not be practicable within the OTS's likely resources. Even so, increasing dialogue between the OTS and those officials within the Treasury and HMRC with responsibility for the development of fresh proposals was expected, in much the same way as consultation took place with the Tax Law Rewrite team.

- 3.2 In 2010, the new government set up the OTS, picking up some but certainly not all of the Tax Reform Commission's ideas. A Joint Parliamentary Select Committee on Taxation was not formed. The OTS was set up as an independent office of HM Treasury. It has a board including its Chair and Tax Director and one senior person from each of HMRC and HM Treasury. The OTS reports to the Chancellor of the Exchequer. The Chancellor is required to lay the OTS's reports before Parliament, and the Chair or Tax Director of the

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<sup>2</sup>[http://conservativehome.blogs.com/torydiary/files/making\\_taxes\\_simpler.pdf](http://conservativehome.blogs.com/torydiary/files/making_taxes_simpler.pdf).

<sup>3</sup>It had previously been suggested by the Conservative Party's Tax Reform Committee.

<sup>4</sup>Ibid., para. 3.3.

OTS may be required to give evidence before the relevant parliamentary committees on the contents of those reports.<sup>5</sup> The OTS sets up Consultative Committees for each project, bringing in the expertise of a varying range of tax professionals, academics and HMRC and HM Treasury representatives. The work is undertaken by a small team of people. The team includes a couple of full-time secondees from HMRC and/or HM Treasury working on projects. These secondees bring a range of skills to the OTS but have not generally had expertise in the areas being worked on, although there is close liaison with the subject specialists in HMRC. In addition, individuals from the tax profession are brought in specifically to use their relevant expertise. Those individuals will generally work one or two days per week for the OTS. On average, there will be the equivalent of five or six full-time people working on the different projects.

- 3.3 The impact of setting up the OTS in this modified way is considered further in Section 7.

#### **4 What is meant by simplification?**

- 4.1 Before assessing the extent to which the OTS has been successful in simplifying the tax system, what is meant by simplification should be addressed. As the Tax Director of OTS, John Whiting, has pointed out, the UK tax system is unlikely ever to be ‘simple’; we live in too complex a world for that.<sup>6</sup>
- 4.2 Many argue, though, about what is meant by simplification and indeed the OTS’s own work on a complexity index has expressly sought to stimulate debate about that very concept.<sup>7</sup> Simplification is more than a matter of reducing the length of tax legislation. While a reduction in the length of the tax code has obvious appeal, short rules do not necessarily equate with simplicity. Short rules can lead to uncertainty. At times, the work of simplification can lead to more legislation rather than less. A notable example from the work of the OTS is found in the changes introduced following its review of share schemes. The fact that a significant amount of legislation was needed to achieve the changes should not detract from the fact that real and practical changes have been made to make the operation of share schemes simpler.

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<sup>5</sup>In practice, such evidence has been rarely called for. The Tax Director has attended the House of Lords Economic Affairs Sub-Committee in relation to IR35.

<sup>6</sup>See, for example, <http://www.accountingweb.co.uk/topic/tax/ciot-s-john-whiting-join-office-tax-simplification/439178> and <https://www.gov.uk/government/news/office-of-tax-simplification>.

<sup>7</sup>[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/285944/OTS\\_Developing\\_a\\_Tax\\_Complexity\\_Index\\_for\\_the\\_UK.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/285944/OTS_Developing_a_Tax_Complexity_Index_for_the_UK.pdf).

However, the current large volume of legislation ‘loses its accessibility and cohesiveness’.<sup>8</sup>

- 4.3 The complexity of the tax system derives not only from the underlying substantive rules but also from the compliance burden resulting from the administration of those rules and the ways in which taxpayers need to make claims, make payments and account for tax due.
- 4.4 What would be expected from simplification is a reduction in the complex interweaving of rules, the number of exceptions and the number of boundaries as well as a reduction in the compliance burden faced by taxpayers. That is the test being applied in this paper. A reduction in the volume of legislation would hopefully be a product of such simplification.

## **5 A summary of the past four years**

- 5.1 In this section, there is an overview of what the OTS has done and a brief summary of how its recommendations have been responded to by government.

### Reliefs

- 5.2 The OTS started by carrying out a review of the reliefs in the tax system.<sup>9</sup> Reliefs can and do contribute to complexity in the system. It was a potentially enormous task: 1,042 reliefs were identified. The OTS excluded reliefs that were subject to international agreements; were ‘structural and an integral part of the tax system’ (for example, provisions to avoid double taxation); were subject to current HMRC/HM Treasury consultations; or were VAT reliefs.<sup>10</sup> Of those remaining, a sample of 155 was analysed in detail. The OTS went back to the policy rationale for their introduction and asked whether the reliefs were still operating within those criteria. In the context of inheritance tax, it was clear that those reliefs could only sensibly be considered in the context of the whole tax.
- 5.3 The result was the recommendation to abolish 47 reliefs on the basis that they were time expired, there was no ongoing policy rationale, the value was negligible or the benefit was outweighed by the administrative burden. It was also recommended that 17 reliefs should be simplified. In addition, key areas of complexity were identified: the problems arising from the two systems of National Insurance and income tax; employee benefits and expenses; inheritance tax and trusts; environmental taxes; and capital gains tax,

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<sup>8</sup>Tax Professionals Forum, *Second Independent Annual Report*, 27 March 2013, [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/204924/taxprofessionalforum\\_270313.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/204924/taxprofessionalforum_270313.pdf).

<sup>9</sup><https://www.gov.uk/government/publications/tax-reliefs-review>.

<sup>10</sup>Because of the interactions between EU law and UK political commitments, and in the light of the EU announcement, on 1 December 2010, that there was to be an evaluation of the current VAT system.

particularly as applicable to companies. Some of these would be returned to later.

- 5.4 Following these recommendations, 7 reliefs that had already expired were abolished in the Finance Act 2011 and another 36 were consulted upon and included in Finance Act 2012. However, for all the reasons the OTS itself had referred to in narrowing its focus for its final recommendations, the reliefs concerned were not core parts of the tax system and the OTS was criticised for picking the low-hanging fruit, although it could be argued that, in fact, the OTS report was realistic. Examples of the reliefs repealed included relief for the first 15p of Luncheon Vouchers – introduced in 1946 at the time of rationing; and relief for trade union subscriptions that were used to pay for superannuation, death benefits or funeral expenses, as pension arrangements now covered the same items. It was a start, but a small one. One of the reasons why more reliefs were not abolished was that consultation responses argued strongly for them to be kept. One particular example of this was the relief for the employee benefit of late-night taxis, where the employers who used this relief most lobbied for it to be kept. Despite the abolition of some reliefs, the 1,042 reliefs at the time of the report soon increased to 1,140.

### Small business

- 5.5 At the same time as reliefs, the OTS was working on an area with potentially much greater ramifications: the taxation of small business.<sup>11</sup> This was a very significant project. The OTS was to examine evidence and identify the areas of the tax system that cause the most day-to-day complexity and uncertainty for small businesses and to recommend priority areas for simplification. Alternatives to IR35<sup>12</sup> were expressly included in the remit.
- 5.6 The result was a set of proposals for the smallest businesses, including a call again for alignment of the income tax and National Insurance systems. More specifically, a new simpler basis for the smallest businesses to calculate their taxable profits was recommended. In brief:
- 5.6.1 Unincorporated businesses that had a turnover of up to £30,000 should calculate their profits using ‘receipts and payments’ (i.e. a cash basis). This would be the default position for these smallest businesses and they would have to opt out to use the existing system. The VAT threshold level was expressly ruled out as the starting point for the legislation but could be an aspiration in the future if the new system worked. This was because those larger businesses were more likely to involve more complex arrangements. To keep the new system simple, it should only apply below the lower threshold.

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<sup>11</sup><https://www.gov.uk/government/publications/small-business-tax-review>.

<sup>12</sup>IR35 deals with the treatment of people working through intermediary companies, such as personal service companies.

- 5.6.2 Simplified arrangements should be introduced for deductions of certain specified business expenses. £5 or £15, depending on the level of use, was suggested for use of the home; other amounts were suggested for expenses such as private use of phones.
- 5.6.3 It was essential that the definition of profit used for tax purposes as a result of these changes should be the same as that used for National Insurance, universal credit and repayment of student loans.
- 5.7 Of particular note is the clear statement made by the OTS:  
We do have an overriding concern about the interaction of any new approach to tax with the proposed Universal Credit. If this is not considered before the finalisation of the Universal Credit rules, and these are based on GAAP<sup>13</sup> profits, any simplification from the use of a turnover-based system for tax will be wasted and worthless for claimants and potential claimants.<sup>14</sup>
- 5.8 The response of government was to introduce what it described as a cash accounting system, but it was for businesses with an income up to £81,000 per year, the VAT threshold. It was not a true cash-in-cash-out system and was far from simple. The simplicity of the proposed system had been eroded by 24 pages of detailed legislation. To what extent this was a result of HMRC and HM Treasury not understanding what the OTS was proposing, or was a result of the increase in the threshold which had in turn led to HMRC being concerned about avoidance, is not clear. Some would say that it was inevitable that the original proposal would be applied more widely if it was to be applied at all. Simplified expenses were introduced but, particularly in relation to home expenses, these were considered to be unrealistically small. In addition, despite the clear statements by the OTS, the profit under these rules would not be the same as the profit calculated under the universal credit rules. Those who could potentially benefit most from a simple system now had to prepare two sets of accounts instead of one if they used the ‘cash’ system.
- 5.9 The Chartered Institute of Taxation (CIOT) summed this up in its response to the Finance Bill provisions:  
For the smallest businesses and particularly for those who are unrepresented, the proposals will be almost impossible to use in practice and carry significant risk of inadvertent compliance failure in relation to the numerous and opaque computational requirements of the legislation.<sup>15</sup>

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<sup>13</sup>Generally accepted accounting principles.

<sup>14</sup>Para. 4.41 of the final report on the taxation of small business:

[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/199180/02\\_ots\\_small\\_business\\_tax\\_review\\_simpler\\_income\\_tax\\_280212.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/199180/02_ots_small_business_tax_review_simpler_income_tax_280212.pdf).

<sup>15</sup><http://www.tax.org.uk/Resources/CIOT/Documents/2013/02/130205%20FB13%20draft%20clauses%20on%20simpler%20income%20tax%20-%20CIOT%20comments.pdf>.

## Employee share schemes

- 5.10 By contrast, the employee share schemes review<sup>16</sup> has been less contentious. In the case of approved share schemes, numerous changes were recommended. Most of them were detailed matters regarding the operation of approved schemes, aligning definitions used in differing approved schemes, dealing with specific events such as retirement, ‘good leavers’ or takeovers, the reinvestment of dividends and the interaction with entrepreneurs’ relief. These changes have been generally welcomed. However, of perhaps greatest impact was a change to self-certification of the schemes.
- 5.11 A report was also published dealing with unapproved share schemes. Following that report, a consultation was run regarding some of the recommendations. These included simplifying the tax treatment of internationally mobile employees who are members of a company share plan, extending corporation tax relief to situations where there is a takeover by an unlisted company and changes to the valuation rules for listed company shares. Again points of detail, albeit important points. A further significant administrative change resulted in allowing the annual returns for such share schemes to be filed online.
- 5.12 Two of the more substantive recommendations, which could potentially have had significant impact on how unapproved share schemes work for employees, led to consultations by the government.<sup>17</sup> The measures concerned the timing of the employee tax charge in relation to certain non-marketable securities and the introduction of a new tax-advantaged ‘employee shareholding vehicle’, through which companies can manage employee share arrangements and create a market for shares. However, the government announced in the Autumn Statement that there was not enough interest in the proposals and, taken together with the significant implementation issues and the potential for abuse, this meant that the proposals would not proceed.<sup>18</sup>

## Pensioners

- 5.13 The pensioners’ tax review also produced a mix of recommendations.<sup>19</sup> However, this project is of particular interest not just in terms of what the final report recommended and what actions government took, but also because of the recommendations in the interim report and the reaction of government.

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<sup>16</sup><https://www.gov.uk/government/publications/employee-share-schemes-review>.

<sup>17</sup><https://www.gov.uk/government/consultations/new-employee-shareholding-vehicle/new-employee-shareholding-vehicle>;  
[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/331816/140717\\_HMRC\\_marketable\\_security\\_consultation\\_final\\_published.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/331816/140717_HMRC_marketable_security_consultation_final_published.pdf).

<sup>18</sup>See letter from David Gauke to the OTS, 3 December 2014,  
[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/384136/FST\\_ltr\\_to\\_OTS\\_re\\_Autumn\\_statement\\_measures.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/384136/FST_ltr_to_OTS_re_Autumn_statement_measures.pdf).

<sup>19</sup><https://www.gov.uk/government/publications/taxation-of-pensioners-review>.

5.14 Dealing first with the interim report, one of the matters raised for consideration was age-related allowances. It seemed that many pensioners were unaware of their need to claim the allowance and that, to taper the allowance, HMRC required many of those with incomes over the income limit to file self-assessment tax returns. The OTS suggested 12 different options for dealing with age-related allowances, one of which was abolition. The report was published in March 2012 just before the Budget. In the Budget, the Chancellor announced that the age-related allowances (ARAs) would be phased out. From April 2013, the ARAs would be frozen at their 2012–13 levels, until the personal allowance caught up. In addition, only existing recipients of the ARAs would be entitled to claim them. The withdrawal of age-related allowances was strongly criticised by some of the bodies representing those affected.<sup>20</sup> Others commented that,

in the course of simplifying one aspect of the tax allowances system, it risks introducing a new set of complexities. ... we will now have a confusing array of age-related allowances fixed by date of birth. We are not sure this is therefore the solution the Office of Tax Simplification might have envisaged when they observed that age allowances are an area of complexity for pensioners. Perhaps the Government would have done better to wait for the OTS's considered recommendation before rushing headlong into legislating.<sup>21</sup>

5.15 In the Treasury Committee's report on the 2012 Budget, the Committee noted that,

having taken the exemplary step of setting up the Office of Tax Simplification the Government took the decision to phase out age related allowances whilst aware that the matter was receiving detailed examination by that body. We hope that in future the Government will take proper recognition of the work of the OTS.

5.16 When it came to publishing the final report in January 2013, the OTS summarised the results of the withdrawal of the age-related allowances in this way:

One personal allowance for all, with the potential elimination of tapering, is clearly a big simplification. It will remove a great deal of confusion, missed claims for the higher allowance and problems with tapering and is therefore something we would support from a simplification point of view. However, we acknowledge there may be interim complexities (and unmet expectations) for those caught in the transition.

5.17 Further recommendations were made in the final report. Some were purely administrative, such as the introduction of an annual statement setting out the amount of taxable income received from the state pension and social security benefits in the tax year. This form – a 'DWP60' – would parallel the P60 that

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<sup>20</sup>See, for example: Age UK response to the Budget, 21 March 2012, <http://www.ageuk.org.uk/latest-news/archive/age-uk-response-to-the-budget/>; 'Budget 2012: personal finance – advisers' view' and 'Pensioners lose age-linked allowance', *Financial Times*, 22 March 2012; 'Is granny's retirement really so taxing?', *Financial Times*, 24 March 2012.

<sup>21</sup>CLOT press notice, 'Simplifying age-related allowances introduces new complexity', 21 March 2012, [http://www.tax.org.uk/media\\_centre/LatestNews-migrated/PR\\_age\\_all\\_complex](http://www.tax.org.uk/media_centre/LatestNews-migrated/PR_age_all_complex).



employers and other pension providers have to give recipients and would ensure pensioners know what taxable income they are receiving. Other administrative recommendations included simplifying the PAYE codes that pensioners receive when they receive numerous forms of income. However, there were also recommendations of a more substantive nature, some of which raised significant policy questions: simplify the married couple's allowance and replace it with a flat-rate payment for those still eligible; abolish the 10% savings rate and use the money saved to increase ISA limits; and revise the blind person's allowance to provide direct grants and support for all those registered blind. Newspaper headlines showed the political minefield involved with change affecting pensioners: 'Pensioners face paying extra tax on savings'.<sup>22</sup> At first, the government response was that the 10% rate would not be abolished. A year later, when the 10% rate was abolished, the same paper ran the headline 'Abolition of 10p rate on savings to benefit pensioners'.<sup>23</sup> The other two substantive recommendations have not been taken further by the government.

- 5.18 The DWP60 was not pursued, on the grounds of cost, with it being argued that the new personal tax statements to be issued to all taxpayers should cover the same ground. Government says that there have been steps taken to improve the flow of information between the Department for Work & Pensions (DWP) and HMRC, and the PAYE coding problem was to be kept under review. More recently, there have been updates on progress on these issues. On the positive side, the OTS has welcomed the increased collaboration between the DWP and HMRC that appears to have developed as a result of the project. On the other hand, the government's general response to the administrative changes – that those changes will be dealt with by digitisation – has not been so welcomed, as many pensioners are 'digitally excluded'.<sup>24</sup>
- 5.19 The government agreed that what it described as 'a little used relief for interest on loans for life annuities taken out by pensioners before April 1999' should be abolished in 2019. It was noted that this would remove a 'significant' number of pages of tax legislation.<sup>25</sup> In fact, following a consultation in the summer of 2013, the decision was taken not to abolish this relief after responses were received indicating that the impact of withdrawal on a small number of elderly and vulnerable people outweighed the benefits of simplification.

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<sup>22</sup>*Daily Telegraph*, 23 January 2013.

<sup>23</sup>*Daily Telegraph*, 23 March 2014.

<sup>24</sup>[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/329890/Pensioners\\_project\\_update\\_Jul\\_14.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/329890/Pensioners_project_update_Jul_14.pdf);  
[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/329892/140402\\_HMRC\\_to\\_OTs\\_Update\\_Final.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/329892/140402_HMRC_to_OTs_Update_Final.pdf).

<sup>25</sup>[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/198501/gov\\_response\\_ots\\_pensioner\\_taxation\\_review.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/198501/gov_response_ots_pensioner_taxation_review.pdf).

5.20 What can be learnt from this project? Overall, a relatively significant simplification for the taxpayers affected was achieved. Wider tax changes – in particular, large increases in personal allowances – came together with the OTS recommendation to phase out age-related allowances without creating real losers or a lengthy transitional period. The initial criticism of the change showed how difficult simplification is when there are potential losers, especially if those losers are a politically important group. That constraint on simplification stopped the life annuities proposals from going through. Interestingly, if the government had waited for the OTS to carry out further work, the opportunity to deal with the age-related allowances might have been lost.

### Employee benefits and expenses

5.21 In 2013, the OTS started work on a project considering the tax treatment of employee benefits and expenses.<sup>26</sup> A range of administrative and substantive proposals were made across three reports.<sup>27</sup> A large number of what were called ‘quick wins’ were included. These mainly dealt with administrative changes or improvement to guidance and most have been pursued by HMRC. The more substantial recommendations have been split between the initial work and some subsequent work, the latter focusing on the treatment of employee accommodation and termination payments. The major administrative recommendations included voluntary payrolling of benefits, meaning that P11Ds would no longer be required, and the extension of PAYE Settlement Agreements (PSAs) under which employers can pay the tax that would otherwise be due from an employee in certain circumstances. Government has said it will consult on the voluntary payrolling. The extension of PSAs is not being pursued. The substantive recommendations again included the alignment of income tax and National Insurance contributions (NICs), consideration of applying the same NICs Class to benefits as to cash, removal of the £8,500 ‘higher-paid employee’ threshold – which gives rise to differing treatment for employees above and below that threshold when receiving certain benefits – reforming the rules for travel and subsistence allowances, providing an exemption for trivial benefits and providing an exemption for certain qualifying business expenses. The government has consulted on the £8,500 limit, trivial benefits and qualifying business expenses. A longer-term review of the treatment of travel and subsistence expenses is being undertaken and the

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<sup>26</sup><https://www.gov.uk/government/publications/employee-benefits-and-expenses-review>.

<sup>27</sup>[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/227088/ots\\_employee\\_benefits\\_interim\\_report.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/227088/ots_employee_benefits_interim_report.pdf);  
[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/275795/PU1616\\_OTs\\_employee\\_benefits\\_final\\_report.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/275795/PU1616_OTs_employee_benefits_final_report.pdf);  
[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/339496/OTS\\_review\\_of\\_employee\\_benefits\\_and\\_expenses\\_final\\_report.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/339496/OTS_review_of_employee_benefits_and_expenses_final_report.pdf).

government issued a call for evidence on employment practices.<sup>28</sup> Nothing has been done in relation to NICs. The government's response to the accommodation and termination payments recommendations is that the proposals are innovative and the reforms would have far-reaching impacts and require careful consideration. The government 'looks forward to considering these issues in the future'.<sup>29</sup> The impression is left that these more radical proposals will go no further in the foreseeable future.

### Partnerships

- 5.22 Also in 2013, the OTS started work on a project considering the tax treatment of partnerships.<sup>30</sup> This was a project designed to look generally at all the tax issues partnerships face, including the issues surrounding limited liability partnerships (LLPs). A series of proposals emerged in the interim report, some administrative and some substantive.<sup>31</sup> While this has resulted in a draft manual of guidance on the taxation of partnerships, it is probably too early to quantify what else will be achieved, as the final report has not been published and there are calls for further evidence. However, one of the main practical recommendations – a call for a more coordinated partnerships team in HMRC – appears to be resisted by HMRC.
- 5.23 Despite the fact that LLPs were included in the remit, the major and controversial anti-avoidance changes announced in December 2013 were not. Neither were the other partnership-related changes announced in September 2013 and December 2013. It is not surprising to see that many people whom the OTS spoke to wanted to comment on those proposals<sup>32</sup> and the implications of the government's approach are discussed in Section 6.

### Complexity

- 5.24 It should also be noted that the OTS has carried out more general work on analysing what causes complexity. The work has resulted in papers considering the impact of the length of legislation and the use and number of definitions.<sup>33</sup> In each of those cases, the conclusion was that each of those factors could contribute to complexity but were not the main drivers of it. The definitions paper was limited in scope by resources and could therefore only consider

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<sup>28</sup><https://www.gov.uk/government/consultations/remuneration-practices-call-for-evidence/remuneration-practices-call-for-evidence>.

<sup>29</sup>Letter from David Gauke to the OTS, 3 December 2014, [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/384136/FST\\_ltr\\_to\\_OTS\\_re\\_Autumn\\_statement\\_measures.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/384136/FST_ltr_to_OTS_re_Autumn_statement_measures.pdf).

<sup>30</sup><https://www.gov.uk/government/publications/partnerships-review>.

<sup>31</sup>[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/274278/PU1619\\_OTS\\_Partnerships\\_Interim\\_report.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/274278/PU1619_OTS_Partnerships_Interim_report.pdf).

<sup>32</sup>See paras 1.7–1.10 of the interim report on partnerships.

<sup>33</sup>[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/193496/ots\\_length\\_legislation\\_paper.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/193496/ots_length_legislation_paper.pdf); <https://www.gov.uk/government/publications/definitions-in-tax-legislation-and-their-contribution-to-complexity>.

three taxing acts. However, it did make some suggestions about steps that could be taken to improve the use of definitions in tax legislation, including consideration of what makes a good definition and the suggestion that a database of definitions should be set up to provide easy access to them for Parliamentary Counsel. Because of time and resource constraints, the OTS's ambitions in this area were limited to future definitions.

- 5.25 One practical result has followed. In the Finance Bill 2014, there is a clause enabling the index of definitions included in an Act to be amended by secondary legislation.<sup>34</sup> As a result of this clause, it should be possible for Parliamentary Counsel to keep schedules of definitions up to date, without having to include legislation in future Finance Bills.
- 5.26 In addition, the OTS has compiled a complexity index,<sup>35</sup> which is designed to identify the most complex parts of the tax rules. The work on the complexity index has been expressly designed to stimulate debate about what complexity is.
- 5.27 Although one practical step was taken as a result of this work, the work generally is designed to suggest ideas and provoke debate and awareness. Government has not formally responded to the work and so, for example, there is no indication that a database of definitions will be produced.

#### Competitiveness; penalties

- 5.28 The two most recent projects to have published final reports are the competitiveness project considering what can be done to further improve the competitiveness of UK tax administration, with particular regard to the World Bank's 'Doing Business' report; and a small scoping project on penalties, considering whether penalties could be made simpler, more consistent and more effective in successfully driving compliant behaviour.
- 5.29 The competitiveness project has set out proposals ranging from some fundamental changes to the taxation of companies by aligning taxable profit and accounting profit more closely, to proposals dealing with administration of the tax system for companies and the ways in which companies can get information and clarification of treatment from HMRC.<sup>36</sup>
- 5.30 The penalties project was very limited in scope. Although the OTS has recommended some administrative changes aimed at improving the way the current system works, the main thrust of the report is to recommend that there should be a much wider post-implementation review of the entire penalties

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<sup>34</sup>Clause 293.

<sup>35</sup><https://www.gov.uk/government/publications/tax-complexity-project>.

<sup>36</sup>[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/362302/competitiveness\\_review\\_final\\_report.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/362302/competitiveness_review_final_report.pdf)

system.<sup>37</sup> That system was introduced after the merger of the Inland Revenue and Customs & Excise in 2005 and is long overdue review.<sup>38</sup>

- 5.31 The initial response of the government to both these reports was published with the Autumn Statement.<sup>39</sup> The more administrative recommendations of the competitiveness report were generally accepted while the more substantive recommendations are for further consideration in the next Parliament. It was stated that the report on penalties was being considered. It is not surprising that little progress in relation to either project will occur before the general election next year.

### Employment status

- 5.32 Finally, there is also the employment status project, which is ongoing and considers the dividing line between employee and self-employed status and whether that continues to be the appropriate distinction to use.

- 5.33 The employment status project has a remit which should be noted. The remit excludes consideration of IR35 and the construction industry scheme. IR35 is excluded because ‘previous OTS work has made recommendations in this area and the government decided how to take the issues forward’. The construction industry scheme (CIS) is excluded because ‘HMRC are also currently consulting on proposals for improving CIS’.<sup>40</sup>

- 5.34 The recommendations regarding IR35 were made in March 2011 and were to abolish or suspend IR35; to introduce a genuine business exclusion; or to improve the administration of IR35.<sup>41</sup> It was recognised that it is not an easy problem to solve and that the only real solution is via tackling the income tax and National Insurance disparity between employed and self-employed. The government said in May 2011 that it would ask HMRC to improve administration.<sup>42</sup>

- 5.35 The exclusions from the remit do raise questions about the way in which the OTS role is viewed by government; this is discussed further in paragraphs 6.14 and 6.15.

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<sup>37</sup>[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/374509/OTS\\_tax\\_penalties\\_final\\_report\\_121114.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/374509/OTS_tax_penalties_final_report_121114.pdf).

<sup>38</sup>See, for example, the commitment to review the system within three years made in the Impact Assessment regarding changes in 2008: <http://www.hmrc.gov.uk/ria/penalties.pdf>.

<sup>39</sup>See letter from David Gauke to the OTS, 3 December 2014, [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/384136/FST\\_ltr\\_to\\_OTS\\_re\\_Autumn\\_statement\\_measures.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/384136/FST_ltr_to_OTS_re_Autumn_statement_measures.pdf).

<sup>40</sup>[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/336877/OTS\\_employment\\_status\\_review\\_terms\\_of\\_reference.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/336877/OTS_employment_status_review_terms_of_reference.pdf).

<sup>41</sup>[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/199183/05\\_ots\\_small\\_business\\_interim\\_report.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/199183/05_ots_small_business_interim_report.pdf).

<sup>42</sup>[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/199184/06\\_ots\\_xstletter\\_small\\_business\\_tax\\_review\\_090511.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/199184/06_ots_xstletter_small_business_tax_review_090511.pdf).

## **6 What do the results of the last four years show?**

- 6.1 In this part of the paper, consideration is given to what can be learnt from the OTS's first four years.

### The approach to simplification

- 6.2 After the initial review of tax reliefs, which possibly emphasised the enormity of the simplification task, the approach of the OTS has been to focus on particular groups of taxpayers (pensioners, employers and employees, small business owners, partnerships) to identify where simplification is possible. Looking at how the tax system works for each particular group does have the advantage of being a practical approach to simplification. One of the strengths of the OTS is its bottom-up approach to simplification. Much of the work involves meeting with as many interested taxpayers and their advisers as possible. The OTS collects information widely about the problems being faced by taxpayers and then explores possible solutions with many of those same people. It consults widely both in terms of the backgrounds of consultees and their geographical location and by actively seeking to ensure that it meets as many representatives of those who will be affected by change as possible. For example, for the project on partnership tax, approximately 50 meetings were held, speaking to nearly 1,000 people. Alongside the external engagement, project teams regularly meet with the relevant experts from HMRC. HM Treasury also contributes to the formulation of proposals.

### The balance between substantive and administrative change

- 6.3 Much of what the OTS has achieved has been concerned with the administration of the tax system: how taxpayers find information, how taxpayers complete returns and what guidance is given by HMRC. These are important elements for simplification and are not to be undervalued. For example, the change to self-certification for approved share schemes has been warmly welcomed by scheme users and advisers. However, such administrative changes often still leave underlying complexities caused by a tangled web of rules. For example, there would undoubtedly be a huge simplification of process for employers, employees and HMRC if 4.4 million P11Ds were no longer necessary but, unless basic rules are tackled, the underlying complexities of the employee benefits and expenses rules will remain.
- 6.4 This is not to say that the OTS has ignored the substantive issues. Its reports have identified significant substantive changes, which have the potential to simplify the system. However, in many cases, the government has chosen not to pursue them. One particular example is the recommendation to align or merge income tax and National Insurance. It is not a new point. Plenty of

others have called for much the same change for many years. The OTS has included it as a recommendation in the reliefs, small business, employee benefits and expenses, and competitiveness reports. Although a consultation on alignment was published in 2011, no real progress has been made on this fundamental problem. The main achievement to date is that Class 2 NICs are to be collected through self-assessment. The government has stated:

In 2011 and 2012 the Government conducted detailed and extensive work with stakeholders regarding the operational integration of income tax and NICs. The outcome of this engagement was to wait until further progress with existing, planned changes to PAYE were made before proceeding further with this work.<sup>43</sup>

This leaves open the question of whether there are plans to do any more in this area. The government's reaction (or, at times, lack of apparent reaction) to many of the OTS's suggestions in this area gives the impression of a lack of government appetite for this fundamental change to the tax system. Perhaps that is not surprising as the evidence of the last 30 years has shown that the practical and political issues concerning the merger of income tax and NICs have outweighed the pressure for simplification.

- 6.5 Some recommendations are acknowledged by government but there is a feeling at times that they may disappear into the long grass, most probably never to appear again. For example, the recommendations made in the employee benefits and expenses report for a more fundamental review of employee benefits and expenses has resulted in a call for evidence issued by HM Treasury. While fundamental changes clearly involve considerable further work after the OTS has produced a recommendation, it is clear from the call for evidence that the ideas will not be going far in the future. The call for evidence states: 'This process is intended to seek views to inform future tax policy development but is not expected to lead directly to any immediate or specific policy outcome'.<sup>44</sup> Similarly, the response to the substantive proposals for dealing with the complexities of the taxation of accommodation and termination payments suggests that reforms in those areas are considered to be too difficult for change realistically to be expected.
- 6.6 This has left the impression on many occasions that the OTS is playing around at the edges. Perhaps it would be more correct to say that government has kept the impact of the OTS's recommendations to the edges. The OTS is given some influence on tackling the symptoms of the problems, particularly when they concern administrative matters, but is kept back from tackling the root causes.

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<sup>43</sup>Letter from David Gauke to the OTS, 19 March 2014, [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/294173/Letter\\_to\\_Michael\\_Jack\\_and\\_John\\_Waiting\\_OTTS.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/294173/Letter_to_Michael_Jack_and_John_Waiting_OTTS.pdf).

<sup>44</sup><https://www.gov.uk/government/consultations/remuneration-practices-call-for-evidence/remuneration-practices-call-for-evidence>.

6.7 Unfortunately, it has not even been the case that all administrative proposals are taken forward or that reasons are given for why they are not. For example, in the second employee benefits and expenses report, the OTS strongly recommended widening the use of PAYE Settlement Agreements. The response is simply that ‘The Government believes that this proposal would not be consistent with the purpose of PSAs’.<sup>45</sup> Even though the OTS has identified this as a potentially huge simplification for employers, there is no explanation of what constraints are preventing this proposal from at least being considered further. The OTS report refers to comments from HMRC regarding the interaction with universal credit. If that is the underlying issue, a fuller response from government would show a more positive engagement with the OTS process.

#### The inability to consider new law

6.8 When an area is being considered by the OTS, it is only permitted to consider the existing law. It is not involved in any changes proposed or brought in during the project. This undermines the credibility of the OTS. If at the same time as the OTS is considering an area the government introduces a change in the same area, the impression is given that the OTS view is not at the heart of the legislative process for tax. The argument often given for lack of consultation on provisions is that the provisions are designed to deal quickly with avoidance.

6.9 One of the most significant examples of this was in the case of the recent partnerships review. When the review was underway, government announced a change to the tax treatment of limited liability partnerships. The concern was that LLPs were being used to provide disguised remuneration to people who were effectively employees without National Insurance being applied. The OTS could not avoid the issue, as is clear from its interim report,<sup>46</sup> but it was not permitted to comment on the proposals save in the most general terms. However, the changes were a distraction from the work of the OTS. Many consultees were concerned about the LLP changes, which had come about suddenly with no consultation and were ill thought through. Not surprisingly, they expected that the OTS would be able to address the issues. At the same time as the OTS was seeking to find ways to simplify the tax treatment of partnerships, the government introduced numerous additional pages of legislation requiring 50 pages of accompanying guidance to try to make it work, but these could not be addressed by the OTS.

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<sup>45</sup>Letter from David Gauke to the OTS, 19 March 2014, [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/294173/Letter\\_to\\_Michael\\_Jack\\_and\\_John\\_Waiting\\_OTS.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/294173/Letter_to_Michael_Jack_and_John_Waiting_OTS.pdf).

<sup>46</sup>See paras 1.7–1.10, [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/274278/PU1619\\_OTP\\_Partnerships\\_Interim\\_report.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/274278/PU1619_OTP_Partnerships_Interim_report.pdf).



- 6.10 The government's intention to introduce the legislation with the Finance Bill on 6 April 2014 gave 'too little time to settle all the outstanding issues, get the legislation right and enable businesses to adapt to that legislation in time for a 6 April start', the Economic Affairs Committee said in its report on the draft Finance Bill 2014.<sup>47</sup> Not only that, but the Committee advocated delay in order to better align the start date with firms' accounting periods so as to reduce the administrative burden on affected partnerships. So while the OTS is attempting to reduce that administrative burden, the government at the same time is increasing it.
- 6.11 Other examples occurred in the context of the employee benefits and expenses review. When that review was well advanced, an interim report having been written and a final one being prepared, a provision was included in the Finance Bill dealing with the benefit of medical treatment in the form of therapies for work-related injuries for a person who is at work. It may have been that the relief was considered appropriate for political or other reasons, but it was an additional complexity in an area that the OTS was actively addressing. It was another example of a piecemeal approach to taxation in this area. At the very least, it would appear more joined up if there had been an explanation with the draft provision of how it fitted into the OTS proposals or why it did not.
- 6.12 A starker example of this problem was seen in the context of the same report in relation to car fuel administration. At the same time as the OTS was preparing its final report covering the administration of matters such as claims for car fuel, a provision was introduced that was expressly contrary to the approach the OTS had already recommended in its interim report. The OTS had recommended a change to reimbursing car fuel by 6 July<sup>48</sup> rather than requiring it to be paid by 5 April (i.e. in year) as the legislation implied. Finance Bill 2014 included a provision requiring payment for private use to be made in the year of the benefit rather than at any time. The CIOT expressed concern that this would be unworkable in cases where it was difficult to compute the private use for a period until the end of that period – the point previously made by the OTS. HMRC rejected the CIOT's calls for an extension to the deadline for making good. However, HMRC has stated that it will consider extending an existing 'administrative easement', under which it accepts payments for the making good of private use of fuel where those payments are made after the end of the tax year but before the P11D has to be filed, to payments for the private use of cars and vans.
- 6.13 Apart from raising issues as to why an unworkable provision that requires an administrative easement is to be introduced, there are clear implications for the

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<sup>47</sup><http://www.publications.parliament.uk/pa/ld201314/ldselect/ldeconaf/146/14602.htm>.

<sup>48</sup>Para. 8.23 of the employee benefits and expenses interim report, <https://www.gov.uk/government/publications/review-of-employee-benefits-and-expenses-interim-report>.

simplification process. At best, this type of situation suggests a lack of communication. At worst, the work of the OTS is undermined – it suggests that there is insufficient buy-in to the simplification process by HMRC, HM Treasury and government. Once more, an explanation of why this provision was introduced when the OTS was advocating a different approach would rebut such inferences.

#### Other limits on remit

- 6.14 The recent statement of the remit for the employment status project raises some further concerns about the limitations placed on what the OTS can consider. In particular, the exclusion of IR35 from a project considering employment status seems surprising. The reason stated is that the OTS previously considered IR35 and made recommendations on which the government took decisions.
- 6.15 There are several problems with the limitation of remit seen with the employment status project. IR35 is core to the issues being considered. Looking again at the issues with IR35 in a different context may result in different feedback from consultations and may result in different ideas coming out of the OTS. Why exclude that possibility? Does it mean that there will be other instances where government excludes core questions because they have been considered before? If so, this leaves a whole raft of other questions, not least as to how long it is before issues can be re-addressed. Surely if there is a fundamental issue that keeps being faced (such as the income tax / National Insurance merger), it undermines OTS work if the OTS is not permitted to repeat or develop ideas? Respect for its work and the thoroughness of its approach risks being undermined.

#### Implementation after reports

- 6.16 When simplification proposals are taken forward, the first step is for HMRC to consult on the changes. This appears to be with no further OTS input, save for the more recent practice of the OTS responding officially itself to consultations.<sup>49</sup> There is no apparent reason for that approach and the experience of the last four years shows how things can go wrong at the implementation stage. From a resource point of view, it seems wasteful. If there is a team of people with expertise who have spent a considerable period of time considering the issues, why not use their expertise again? Aside from the waste of valuable resources (especially considering HMRC's limited resources), consultees are frustrated by finding that issues they have raised are ignored. At worst, the simplification proposals are taken forward incorrectly and the situation can be made worse.

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<sup>49</sup>[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/330003/Note\\_on\\_HMRC\\_condocs\\_published\\_180614.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/330003/Note_on_HMRC_condocs_published_180614.pdf).

- 6.17 The introduction of the cash basis for small business illustrates the problems. The changes introduced were fundamentally different from those recommended by the OTS, and what was proposed as a simplification resulted in what has generally been perceived as an added complication. Clear statements as to why the threshold should be very low and the need to tie in the new calculation with the calculations used by the DWP were apparently ignored. As a result, there is a risk that, despite the length of the eventual legislation (and possibly because of it), and because of the higher amounts at stake, there is an increased likelihood of abuse, possibly requiring yet further legislation and further complexity in years to come. Some argue that this outcome was inevitable and that a more fundamental overhaul and simplification of the taxation of small business is required. However, the disconnect between what was proposed and what was implemented is a concern.
- 6.18 The cash basis problems were the most significant example of the problems with implementation, but they were not the only one over the past four years. Even where the government has apparently decided to implement the recommendations and the changes are less contentious, implementation has not been as effective as it might have been. There is no apparent justification for some of the changes between what the OTS recommended and what was in fact done. For example, in the context of the changes to share schemes for internationally mobile employees, the draft legislation does not wholly meet the recommendations of the OTS, particularly with regard to its recommendation that general earnings principles should be adopted. Again in the context of share schemes, the decision to implement changes from 1 September 2014 rather than the start of the 2015–16 tax year may lead to difficulties for employers in terms of tax and social security withholdings for award grants before and after 1 September. This may significantly increase the administration and reporting requirements in the tax year 2014–15.
- 6.19 The implications of this extend beyond the actual rules that are changed. The value of the OTS's work is seriously undermined if its recommendations, based upon considerable work and consultation, are apparently ignored or overridden without reasoned explanation and without taking into account the limits proposed by the OTS. In addition, the government's tax-policy-making strategy is undermined if it appears that, following consultations – whether by OTS or otherwise – proposals are taken forward by HMRC and/or HM Treasury personnel with insufficient understanding of the issues involved. In the case of the small business changes, it may have been thought that, despite the OTS's advice, it would aid simplification to use the VAT threshold from the start, but the impression given has been that those who pursued this approach did not understand the ramifications of so doing. The OTS proposal was for a

simplified basis of taxation with little risk to the exchequer because of the low threshold, which could have been simply explained. When the details and complexities of the draft legislation, with all its additions to the basic idea, were seen, the result was very different from the one originally proposed. It has been a concern of many since the formation of the OTS (including the Tax Law Review Committee) that, for the OTS to be truly effective, it should be involved in the development of its recommendations, so that the OTS's expertise and knowledge can be used to the full and there is consistency in tax policy making.

## **7 Implications for the future**

- 7.1 The OTS's achievements to date are welcome but there is much left to do. The OTS offers the potential for more simplification of the UK tax system; but for the simplification to be more substantial, lessons should be learnt from the past four years in going forward.
- 7.2 The bottom-up consultative approach of the OTS is a great strength of its work. Often, the OTS will consult more widely than HMRC. It will actively seek out potentially interested people and it travels around the country to obtain views. In contrast, at times, HMRC is criticised for being too reliant on too few participants in consultation.
- 7.3 However, it is the way in which government views and reacts to its work that is key to it achieving more.
- 7.4 The relationship between the OTS's work and tax policy making is key. Simplification needs to run hand in hand with tax policy making. The questions at the heart of the process should include considering what the policy is and should be in an area and how that can be delivered as simply as possible. As was stated at the OTS's own review of its first few years, 'OTS work needs to be more embedded into the policy making process – and not be seen as an add-on at the end'.<sup>50</sup> This means that when the OTS is reviewing an area, it should be looking at the entire area. If government proposes changes to an area under consideration by the OTS, those changes should await the outcome of the report from the OTS whenever possible. If a change will be introduced that will conflict with a recommendation in a report, an explanation of why the change will proceed despite the recommendation would show that the OTS's work is being taken into account and would show a more coherent approach.
- 7.5 As a practical matter, it would seem that communication about what the OTS is doing and what its recommendations are could be better disseminated within HMRC.

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<sup>50</sup><http://taxsimplificationblog.files.wordpress.com/2013/07/workshop-readout1.pdf>.

- 7.6 Recognition of the ties between simplification and policy may act as a discipline to make government wary of latching onto suggestions individually and before full consideration. Similarly, claims that the advantage of a change is that it removes several pages of legislation miss the real point of simplification and are too easily attacked by commentators, who point to the hundreds of new pages of legislation added with each Finance Act.
- 7.7 If a recommendation is taken forward, implementation is a vital stage, when, as experience shows, things can go wrong. It would appear that many of the problems might have been avoided if the OTS had been kept involved throughout implementation, working with HMRC and HM Treasury to develop the consultations, reach conclusions and implement change through legislative drafting. To the extent that changes, whether at the consultative stage or later, differ from the OTS recommendation, a clear explanation of why would improve the standing of OTS's work.
- 7.8 Further thought should also be given to the status and independence of the OTS. Although it is described as an independent office of the Treasury, the OTS works in close collaboration with HMRC and HM Treasury. This is a significant advantage. There is no point in the OTS producing recommendations that will not work for either HMRC or HM Treasury. That does not mean that the OTS is directed by HMRC or HM Treasury, but the close collaboration means that the feasibility of proposals can be explored to an extent. Tax simplification cannot be dealt with in a vacuum. The simplest way of taxing something may be politically unpalatable and clearly the OTS has to recognise this practical problem. Indeed, the collaboration could be expected to imply that there is some element of support for the proposals when actually published, both with the departments and within government. Yet, too often, too little of what is proposed by the OTS is taken forward.
- 7.9 As a physical matter, the OTS is located in the Treasury building. Its board members include some of the most senior people in HMRC and HM Treasury. The perception can be that it is not sufficiently independent of HM Treasury. Yet it is treated as being independent by HM Treasury and HMRC; for example, HM Treasury and HMRC will not share their own policy work with the OTS. The OTS comes to its projects unencumbered by such work. However, the OTS is bound by the Finance Bill and Budget processes. The government clearly wants to make announcements at regular intervals in that cycle to show that something is happening, and there is evident pressure to produce what are described as 'quick wins'.
- 7.10 In contrast, the Office for Budget Responsibility (OBR) is located outside the Treasury and is a truly independent body, albeit that in order to carry out its

work it is necessary for the OBR to work together with HM Treasury, HMRC and DWP. However, this is an information-based cooperation.<sup>51</sup>

- 7.11 The Law Commission was established by Parliament in 1965 as a statutory independent body. The Commission submits ‘programmes for the examination of different branches of the law’ to the Lord Chancellor for his approval before undertaking new work. Before deciding which projects to take forward, the Law Commission takes views from judges, lawyers, government departments, the voluntary and business sectors, and the general public. The Commission also takes on projects that are referred to it by government departments. Once the Law Commission has agreed to review an area of law, the remit of the project is decided, in conjunction with the relevant government department.<sup>52</sup> This is not dissimilar to the OTS, yet the Law Commission is seen as much more independent of government than the OTS and as more authoritative.
- 7.12 Would the OTS benefit from being perceived as more independent? Possibly yes, but independence can have advantages and disadvantages. The collaboration with HMRC and HM Treasury can be of huge value and should be preserved. Greater benefit may be achieved by addressing the status government and Parliament give to the OTS’s work, wherever it is located and regardless of the extent of its independence.
- 7.13 When first proposed, the OTS was to be a body reporting to a Joint Parliamentary Select Committee on Taxation. It would not simply report to the Chancellor. Although the Chancellor lays the reports before Parliament and the OTS can be called to give evidence to Parliamentary Committees, the loss of the Joint Parliamentary Committee is real. The Committee was supposed to be a body that would significantly improve the scrutiny of government initiatives and proposals and would receive written and oral evidence from external experts. It would also examine and make recommendations on proposals presented to it by the OTS. Such a committee could have been a stronger driver of simplification. The added level of scrutiny of response to recommendations could be beneficial. In addition, the Committee could hold HMRC and HM Treasury to account for the response to the OTS’s reports. Both HMRC and HM Treasury are organisations with significant pressure on their resources. It would not be surprising if their preference is for maintaining the status quo rather than pushing forward significant change. The Committee would have the potential to overcome the force of inertia.
- 7.14 If the OTS in the future continues to report to the Chancellor and there is no Parliamentary Committee to drive the process, the status that government attaches to the OTS’s recommendations needs to be greater. The

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<sup>51</sup>See the OBR Memorandum of Understanding, <http://budgetresponsibility.org.uk/independence/working-with-government/>.

<sup>52</sup><http://lawcommission.justice.gov.uk/about/how-we-work.htm>.

recommendations should not be something to be ignored without explanation. The government of the time should support the work of the OTS sufficiently to be prepared either to take forward recommendations or to explain why not. Cherry-picking the easier changes undermines the standing of the OTS and suggests a lack of commitment to simplification.

7.15 Professor Freedman goes further, arguing for the OTS to become the Office of Tax Policy advising on policy but recognising that policy decisions remain with Parliament.<sup>53</sup> Whether or not this occurs, the interaction between the work of the OTS and policy making needs to be recognised.

7.16 Finally, there is the question of resources. The OTS is currently a small office for the size of its task. It has produced a remarkable amount for its size in the past four years. If the status of its recommendations is improved and there is therefore a greater sign of commitment to the simplification process, an increase in resources would seem appropriate to enable it to do more, more quickly. There has been notable criticism of its understaffing:

The Office of Tax Simplification is grossly understaffed and has focused on abolishing tax rules that are no longer necessary, rather than more radical simplification. HM Treasury and HMRC should work together to make more radical progress in simplifying the UK's tax code, and should equip the Office of Tax Simplification with the resources and influence it needs to help them do so.<sup>54</sup>

The remarks were made without speaking to the OTS and failed to take into account that, by that stage, the OTS had considered the merger of income tax and National Insurance, recommended the suspension of IR35 and proposed the new cash basis for small business. They also failed to take into account the role of Ministers in setting the agenda for tax simplification. However, the basic point that the OTS is under-resourced is sound.

7.17 Increased consideration could also be given to whether secondees from HMRC and HM Treasury should include area specialists. Work such as tax simplification relies on a high level of technical expertise, and being able to use more of the expertise within HMRC and HM Treasury would be an advantage and offer the potential for increased efficiency.

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<sup>53</sup>[http://www.sbs.ox.ac.uk/sites/default/files/Business\\_Taxation/Docs/Publications/Policy\\_Papers/creating-new-UK-institutions-for-tax-governance\\_0.pdf](http://www.sbs.ox.ac.uk/sites/default/files/Business_Taxation/Docs/Publications/Policy_Papers/creating-new-UK-institutions-for-tax-governance_0.pdf).

<sup>54</sup>Committee of Public Accounts, *Tax Avoidance: The Role of Large Accountancy Firms*, Forty-Fourth Report of Session 2012–13, HC 870, 26 April 2013, <http://www.publications.parliament.uk/pa/cm201213/cmselect/cmpubacc/870/870.pdf>.