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Economic Affairs Committee

2nd Report of Session 2015–16

The Draft Finance Bill 2016

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Select Committee on Economic Affairs

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The Members of the Sub-Committee which carried out this inquiry (The Finance Bill Sub-Committee) are:

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*Lord Monks was unable to attend most meetings.

Declaration of interests

See Appendix 1.

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Q in footnotes refers to a question in oral evidence.

SUMMARY

The Finance Bill Sub-Committee of the Economic Affairs Committee has met most years since 2003 to examine selected aspects of the year's Finance Bill or, since 2013, draft Finance Bill.

The FBSC began its inquiry into the draft Finance Bill 2016 in January and chose to focus on two cross-cutting issues: the extent to which measures proposed in the draft Bill contribute to the simplification of the personal tax system; and their impact on the compliance burdens of taxpayers. In considering these two broad issues, the inquiry concentrated on three areas in the draft Bill: the clauses reforming the taxation of savings income and dividends; those providing new powers for HMRC to issue Simple Assessments of an individual's tax liability; and those establishing the Office of Tax Simplification (OTS) on a statutory basis.

Our conclusions and recommendations are set out in detail in the final chapter of our report. They cover six broad areas of concern which arise not only in the context of the individual topics under investigation but apply also to the development, communication and implementation of tax policy in general:

- **Consultation:** the consultation required by the 'new approach' to tax policy making is not being carried out consistently. This is a matter of regret. The lack of consultation has resulted in opportunities to reduce the amount of complexity apparent in the design and implementation of the proposed changes being missed.

- **Communication**: significant changes to the taxation of savings and dividends will come into effect in a matter of weeks. Many, perhaps most, taxpayers are unaware of this. The Government must take responsibility for notifying taxpayers directly of these changes. HMRC's current communications strategy is simply inadequate.

- **Strategy**: the absence of a roadmap for changes to the taxation of savings and dividends is disappointing and the resulting confusion hinders taxpayers' ability to plan for the longer term.

- **Digital Accounts**: the move to digital accounts should be undertaken cautiously. The Government must consult fully and ensure that businesses and individuals are helped, not hindered, by the new system.

- **Complexity**: the complexity of the tax system and the compliance burden placed on many individual taxpayers is growing. The Government must do more to demonstrate how it is delivering a simpler tax system.

- **Scrutiny**: there must be robust scrutiny—in the form of a post-implementation review—of all major tax reforms undertaken by HMRC, and the findings of these reviews must be published.

The Taxation of Savings and Dividends

The draft Bill establishes a new Personal Savings Allowance, which will mean the majority of individuals will pay no tax on their savings income, whilst also abolishing the Tax Deduction Scheme for Interest so that interest will generally

be paid gross rather than net of 20% basic rate tax. The tax free amount is up to £1,000 depending on income. A new dividend allowance likewise removes the tax charge on the first £5,000 of dividends, and the Bill also introduces new dividend tax rates and abolishes the complex dividend tax credit system. All changes take effect from 6 April 2016.

The evidence submitted to the inquiry painted a mixed picture on simplification. Taken together, these changes were seen to simplify the tax affairs of many taxpayers, particularly those whose savings or dividend income is taken out of tax altogether. However, higher and additional rate taxpayers face additional complexities because the structure of the new allowances creates cliff edges, which mean that an additional £1 of savings income can result in the loss of £500-worth of savings allowance. It also produces awkward interactions with an already highly complex personal tax system. Compliance burdens increase for some basic rate taxpayers who will have to consider whether they need to notify HMRC and pay tax on their savings and dividend income paid gross whereas their tax liability is currently covered by deduction at source or the dividend tax credit. There is considerable evidence that taxpayers are generally not very aware of their current tax obligations. Finally, the introduction of the new allowances will complicate personal financial decisions and require a review of profit extraction strategies by shareholder/directors of small companies.

We share the concerns of our witnesses about these proposals. We are disappointed by the absence of consultation on these substantial reforms which affect millions of taxpayers. We are also concerned at the lack of a communication strategy to inform taxpayers of the fundamental changes that are due to take effect within weeks. We have recommended that HMRC urgently develop a comprehensive strategy to make taxpayers aware of these changes and how they will affect their tax obligations and financial decisions.

Simple Assessments and Making Tax Digital

The draft Bill also enables HMRC to issue a legally enforceable assessment of an individual's tax liability based on information supplied by employers, pension providers, banks and other third parties. We agree with our witnesses that this change is to be welcomed because it has the potential to reduce the compliance burden of taxpayers with relatively straightforward affairs for whom these 'Simple Assessments' will replace Self Assessment tax returns. However, we share concerns about the quality of third party data on which such assessments would be based and about taxpayer awareness of their obligation to check and, if necessary, dispute their assessments within a short 30-day time limit. Accordingly, we make recommendations about assuring data quality and clarifying and publicising the responsibilities of taxpayers receiving Simple Assessments.

Simple Assessments were presented as the first step towards a system of digital tax accounts that will replace tax returns by 2020. Whilst generally embracing digital advances in the tax system, most evidence suggested proceeding with caution. It exposed concerns about the ability of HMRC to implement the new IT systems successfully and the lack of preparedness of some taxpayers, especially the 'digitally excluded', to deal with digital systems. Many witnesses were particularly anxious about the proposal that all businesses should keep their income and expenditure records in digital form and update HMRC quarterly. The Government will be consulting on these proposals in the course of 2016 and we recommend that the consultations should address the significant concerns expressed by small businesses.

Office of Tax Simplification

The draft Bill also establishes the OTS as a permanent office of HM Treasury and defines its role and functions. This proposal was welcomed by our witnesses who all praised the past work of the OTS, but they had concerns about the resourcing and independence of the OTS and about the relatively narrow functions assigned to it by the draft legislation. We share many of these concerns, and we make recommendations that the OTS should be properly resourced, integrated into the tax policy development process, and should report on overall progress towards a simpler tax system.

The Draft Finance Bill 2016

CHAPTER 1: INTRODUCTION

1. This is the eleventh report in a series which began in 2003 when the House of Lords Select Committee on Economic Affairs first appointed a Sub-Committee to inquire into selected aspects of that year's Finance Bill. The Finance Bill Sub-Committee's inquiries address technical issues of tax administration, clarification and simplification, rather than rates or incidence of tax.

2. The Economic Affairs Committee publishes the report drawn up by its Sub-Committee on the draft Finance Bill before the Budget and publication of the Finance Bill itself. This enables the report to be available for consideration at all stages of the Parliamentary process.

3. The draft Finance Bill 2016 was published on 9 December 2015 and the Sub-Committee began its inquiry on 13 January 2016.

4. This year, the Sub-Committee decided to concentrate its inquiry on two cross-cutting issues: the extent to which the measures proposed in the draft Finance Bill contribute to the simplification of the personal tax system and their impact on the compliance burdens of taxpayers. The inquiry was with reference to three specific topics.

5. The first topic covered the proposed changes to the taxation of savings interest and dividends, including the abolition of the Tax Deduction Scheme for Interest (TDSI) and dividend tax credits.

6. The second topic concerned new powers for HM Revenue and Customs (HMRC) to issue Simple Assessments. This is HMRC's first step in its five year plan for '*Making Tax Digital*'. Although most of the statutory provisions to implement those plans are expected to be in the Finance Bill 2017, there is already considerable public interest in this area, including from our witnesses. As a result the inquiry looked beyond the clauses in the current draft Finance Bill and this Report considers emerging concerns about HMRC's plans and suggests areas for inclusion in forthcoming consultations.

7. The third topic concerned the proposals to put the Office of Tax Simplification (OTS) on a statutory footing and confirm its status as an independent office of HM Treasury.

8. As in previous years, the Sub-Committee conducted its inquiry by taking written and oral evidence from leading professional and business organisations, academia, the financial services sector and professional firms, as well as from HM Treasury, HMRC and the OTS. A list of those who have contributed to the inquiry in this way is given in Appendix 2. The Sub-Committee would like to thank all those who have contributed to its work.

9. The Sub-Committee's findings on the three chosen topics are in Chapters 2 to 5 and those on the cross-cutting issues in Chapter 6.

CHAPTER 2: THE TAXATION OF SAVINGS INCOME

10. This chapter covers two measures in the draft Finance Bill 2016: the introduction of the Personal Savings Allowance and the abolition of the Tax Deduction Scheme for Interest (TDSI). To set the scene for these reforms, the chapter begins with a brief description of the position in 2014/15, prior to the changes to the taxation of interest announced in the 2014 and 2015 Budgets. It then considers the draft Clauses (1 and 4) directly covered by this inquiry which give effect to announcements made in the March 2015 Budget.

11. The new Personal Savings Allowance and the abolition of the TDSI will both take effect from 6 April 2016.

Position prior to 2014/15

Taxation of savings income

12. All savings income, including interest on deposits held with banks, building societies and other financial institution, was taxable at the taxpayer's marginal rate of tax (20%, 40% or 45%) except where that interest income:

(a) derived from savings held in a cash Individual Savings Account (ISA)[1]; or

(b) came from savings outside an ISA but was fully covered by the Personal Allowance because the taxpayer's total income amounted to no more than £10,000, the value of the Personal Allowance for 2014/15[2]; or

(c) was non-ISA interest that was covered by the 10% starting rate for savings income which applied to interest below the starting rate limit of £2,880. The rules for determining whether the starting rate applies are quite complicated, but they meant that in 2014/15 anyone with a total income below £12,880 paid income tax at 10% rather than 20% on their savings income.

Tax collection

13. Under the TDSI banks, building societies and most other deposit takers are obliged to deduct income tax at 20% from any interest they pay to individuals, trusts and partnerships and pay it over to HMRC.[3] The TDSI covers most, but not all, savings income. Various other tax deduction arrangements apply to savings income not covered by the TDSI such as income arising from collective investment schemes, including bond funds, unit trusts and open-ended investment companies, or as part of compensation payments from banks and building societies.

14. Any institution paying interest from which tax has been deducted must provide HMRC with information about the recipient of the interest and the

1 The annual cash ISA subscription limit for 2014/15 was £5940. The March 2014 Budget announced a single subscription limit of £15,000 for cash and equity ISAs with complete transferability between them.
2 The age-related personal allowance is higher, at up to £10,660 for 2014/15.
3 Income Tax Act 2007, Part 15, Chapter 2, sections 850–873

tax deducted from it,[4] and the recipient with information about the interest paid and the tax deducted from it.[5]

15. These tax deduction at source arrangements mean that basic rate taxpayers do not generally need to report interest income to HMRC (unless they complete a tax return), but higher and additional rate taxpayers do in order to pay the difference between the tax due at their marginal rate and the tax already deducted. Those who expect to have no tax liability can apply to their bank to have their interest paid gross by completing form R85, and those who want to claim back overpayments of tax can apply to HMRC using form R40.

Changes announced in March 2014 Budget

16. In the March 2014 Budget the Chancellor announced that from 6 April 2015, the starting rate for savings income would be reduced from 10% to 0% and the starting rate limit for savings income would be extended to £5,000.

17. The changes to the starting rate for savings income were enacted in the Finance Act 2014. As a result anyone with an income not exceeding the personal allowance plus £5,000 (£15,600 in 2015/16) pays no tax on any interest they receive on savings held outside an ISA.

18. The March 2014 Budget changes were estimated to cost the Exchequer £135m in 2015/16, rising to £355m in 2018/19.[6] The savings rate changes were estimated to benefit up to 1.5 million individuals provided they applied to have their interest paid gross or claimed any overpayments of tax deducted at source.

Changes announced in March 2015 Budget

19. In the March 2015 Budget the Chancellor announced (with effect from 6 April 2016):

(a) the introduction of a new tax allowance for savings income, the Personal Savings Allowance, covering £1,000 of savings income for those who paid tax at the basic rate and £500 for higher rate taxpayers. It would not be available to additional rate payers; and

(b) the abolition of the obligation to deduct tax under the TDSI so that most interest would be paid gross, although the obligation to provide information to HMRC would remain.[7]

20. The new Personal Savings Allowance would be worth up to £200 per year in reduced tax on savings income to basic and higher rate taxpayers. Since the starting rate for the savings nil rate band remained in place, the introduction of the Personal Savings Allowance would mean that in 2016/17 no tax would be due on savings income if a saver's total income was below £16,800.[8]

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4 Income Tax Act 2007, section 851
5 Income Tax Act 2007, section 975
6 HM Treasury, *Budget 2014: policy costings*, March 2014, p 6: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/295067/PU1638_policy_costings_bud_2014_with_correction_slip.pdf [accessed February 2016]
7 Finance Act 2011, schedule 23 para 12
8 The Summer Budget 2015 raised the Personal Allowance to £10,800 for 2016/17 and held the ISA limit at £15,240, the same as for 2015/16.

21. The Government estimated that, taken together with the changes to the ISA rules, 95% of taxpayers would pay no tax on their savings income and "there will be no additional tax costs for any savers."[9] Some 1.4 million individuals, mainly additional rate taxpayers and those with above average savings, would still have some tax to pay on their savings income. As far as possible, HMRC intended to collect this tax through the PAYE system on the basis of information provided by banks and other third parties. Exchequer costs from 2016/17 to 2019/20 were estimated to be £1,030m, £565m, £640m and £765m.[10]

Consultation on options for non-TDSI Savings Income

22. An HMRC document was published in July 2015 consulting on options for dealing with other, non-TDSI, deduction at source arrangements in such a way as to balance the interests of savers, financial institutions and the Exchequer.[11] This floated a number of options including retaining the current deduction arrangements for non-TDSI interest; removing them for all non-TDSI interest; removing them below a specified limit; and allowing individuals to choose whether to receive such interest gross or net of tax.

23. HMRC received 51 responses to its consultation. The Government concluded that the consultation did not point to a clear way forward and that, for most non-TDSI savings income, the issue was best left to be addressed once further progress had been made on the design and implementation of the new digital tax accounts.[12] However, in its response, the Government added that it had,

> "not yet reached a decision on this question in respect of authorised investment funds, investment trusts and P2P (peer to peer) lending. The government is continuing to analyse information provided to understand fully the impact of potential changes, and an announcement will be made as soon as possible."[13]

The draft legislation

24. Draft Clause 1 amends the Income Tax Act 2007 to establish a new nil rate tax band for savings income falling within an individual's annual Personal Savings Allowance and to provide rules determining the amount of an individual's Personal Savings Allowance entitlement, which may be £1,000, £500 or £0 according to whether they have any income for that year liable to higher rate tax or to additional rate tax. It also defines 'savings income' and provides that income from an ISA or income which qualifies for the 0% starting rate for savings income (introduced by the Finance Act

9 HMRC and HM Treasury, *Overview of Legislation in Draft* ,December 2015, p 31: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/484588/OLD.pdf [accessed February 2016]

10 HMRC, *Policy Paper, Income Tax: Personal Savings Allowance*, December 2015: https://www.gov.uk/government/publications/income-tax-personal-savings-allowance/income-tax-personal-savings-allowance [accessed February 2016]

11 HMRC, *Consultation Document, Deduction of income tax from savings income: implementation of the Personal Savings Allowance*, July 2015: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/444945/Deduction_of_income_tax_from_savings_income_-_implementation_of_the_Personal_Savings_Allowance.pdf [accessed February 2016]

12 HMRC, *Deduction of income tax from savings income: implementation of the Personal Savings Allowance: A Summary of Responses*, December 2015, paras 3.2–3.7: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/495640/Deduction_of_income_tax_from_savings_income_implementation_of_the_Personal_Savings_Allowance.pdf [accessed February 2016]

13 ibid, para 3.9

2014) does not use up any of an individual's Personal Savings Allowance. However, savings income that falls within the Personal Savings Allowance will continue to count as taxable income for the purposes of determining the individual's marginal tax rate and their basic or higher rate limits and so determine their entitlement to income tax allowances.

25. Draft Clause 4 introduces the Schedule which amends the Income Tax Act 2007 to remove the obligation (under the TDSI) of banks, building societies and other institutions to deduct income tax from the interest or other returns they pay on certain savings and investments.

Guarded welcome for proposed changes

Simpler for most taxpayers

26. Those organisations submitting evidence to our inquiry generally welcomed the changes introduced by these draft clauses. The Building Societies Association submission was fairly typical in writing that "the removal of 95% of customers from savings income tax is clearly welcome for building society customers and for the general economy in which the sector operates."[14] In a similar vein, Grace Stevens, of the Legal & General Group, commented that "for the vast majority of savers this will be a simplification and they will be able to take full advantage of the allowances."[15]

27. Organisations advising those on relatively low incomes were particularly enthusiastic about the change. Caroline Miskin, representing TaxAid, an organisation which provides advice to low income taxpayers, stated:

> "We very much welcome this move because of its impact on low-income savers, who will no longer have to complete R85 forms with their bank, or think about whether they need to or not. Many more will no longer have to fill in annual R40 forms to reclaim tax. This will address the issue that many savers do not reclaim tax to which they are entitled."[16]

28. Robin Williamson, of the Low Incomes Tax Reform Group agreed: "It is a generally welcome development. Having people whose savings income is relatively modest taken out of tax is a simplification, if it is well handled, and welcome in itself."[17]

But more complex for many

29. It was also widely felt that, while the changes simplified the tax affairs of the majority of tax payers who have a relatively small amount of savings income, they added complexity and compliance costs for those with larger amounts or those on higher incomes. John Whiting, Tax Director for the Office of Tax Simplification, remarked that, although he welcomed what was a simplification for most people, he questioned the how exactly it was being done.[18]

30. The additional complexities and compliance burdens were seen to arise from four distinct sources. The first of these is that the changes have the effect of imposing new reporting and taxpaying obligations on basic-rate taxpayers

14 Written evidence from the Building Societies Association (FBB0015)
15 Q 46 (Grace Stevens)
16 Q 25 (Caroline Miskin)
17 Q 25 (Robin Williamson)
18 Q 64 (John Whiting)

whose savings income exceeds the Personal Savings Allowance, who had previously received interest after deduction of tax. As Frank Haskew, from the Institute of Chartered Accountants of England and Wales, put it: "At the moment, in practical terms, basic rate taxpayers have nothing to worry about, whereas under this system, potentially, they will have much more to worry about and might have to pay some tax as a result."[19]

31. HMRC told us that most of these cases will be dealt with through PAYE coding adjustments,[20] but, as Mr Whiting pointed out, this is not a complete answer.[21] Emma Churchill, from HMRC provided some reassurance:

> "There will be a very small number—our current estimate is that it will be in the low thousands—for whom we will not be able to code out the tax that they owe, and don't currently fill in tax returns, and we will need to inform them of that … We will either write to them or if they are in a personal tax account, indicate to them through their personal tax account that an amount of tax is owing … Of course, they all have a wide variety of options for payment of that tax."[22]

32. The Chartered Institute of Taxation also pointed out, in its written submission, that, while trustees and personal representatives are not entitled to the Personal Savings Allowance, many will find themselves with similar new burdens in that, from April 2016, they will receive savings income gross which was previously paid under deduction of tax.[23] HMRC's assessment of the Personal Savings Allowance, published alongside the draft Finance Bill, recognises this issue and promises an update later this year.[24]

33. The second source of complexity is that, as explained in paragraph 13 above, not all savings income eligible for the Personal Savings Allowance will be paid gross. Deloitte noted that, as a result, "from 6 April 2016 two sources of income which a taxpayer might consider to be similar will have different withholding obligations, thus leading to confusion amongst taxpayers."[25] The Building Societies Association[26] and the British Bankers' Association[27] submissions to the Sub-Committee made similar points.

34. The third area of complexity is that the Personal Savings Allowance, alongside ISAs and the starting rate for savings income, presents individuals trying to decide how to invest their savings in a tax-efficient way with a confusing array of seemingly overlapping choices. Mr Whiting of the Office of Tax Simplification questioned whether it was worth keeping the starting rate for savings income if you were introducing the Personal Savings Allowance. EY remarked, in their written evidence, that the introduction of the Personal

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19 Q 1 (Frank Haskew)
20 Q 86 (Brian Redford) and HMRC, *Income Tax: Personal Savings Allowance*, 9 December 2015: https://www.gov.uk/government/publications/income-tax-personal-savings-allowance/income-tax-personal-savings-allowance#contents [accessed February 2016]
21 Q 64 (John Whiting)
22 Q 86 (Emma Churchill)
23 Written evidence from the Chartered Institute of Taxation (FBB0003)
24 HMRC, *Income Tax: Personal Savings Allowance*, 9 December 2015: https://www.gov.uk/government/publications/income-tax-personal-savings-allowance/income-tax-personal-savings-allowance#contents [accessed February 2016]
25 Written evidence from Deloitte LLP (FBB0004)
26 Written evidence from the Building Societies Association (FBB0015)
27 Written evidence from the British Bankers' Association (FBB0005)

Savings Allowance "may distort the current incentives for some forms of saving, since this will reduce the benefit of holding cash in a Cash ISA."[28]

35. Several witnesses commented that the frequent Budget changes to savings income taxation, including pensions, on an apparently piecemeal basis, created confusion, instability and uncertainty for savers. This was exacerbated by a lack of clarity about the long-term direction of savings policy. That could be remedied by the publication of an outline of the Government's longer-term strategy for the taxation of savings income. John Cullinane, from the Chartered Institute of Taxation, commented: "We do not really know what the destination is because there is not a roadmap."[29]

36. Cerys MacDonald, of HM Treasury accepted that greater clarity might be needed, saying that HM Treasury and HMRC should "look at the material that is available in the public domain so that it covers the entire landscape and is written through the eyes of a particular individual rather than through the eyes of a particular fiscal event."[30] In response to a question about the continued relevance of ISAs for the majority of taxpayers with relatively small savings, Ms MacDonald emphasised that the task was to "provide the right information to allow people to make those informed choices, but it is not for the Government to direct individuals towards a particular savings strategy."[31]

37. The fourth source of complication for savers was the way in which the Personal Savings Allowance has been designed: it will introduce cliff edges where entitlement falls from £1,000 to £500 and from £500 to nothing; and savings income covered by the Personal Savings Allowance will continue to count as taxable income for the purposes of calculating liability to the higher and additional rates of income tax. Taken together with existing tapers and cliff edges, these taxpayers could find it hard to see the introduction of the Personal Savings Allowance and the abolition of the TDSI as straightforward simplifications.

38. As Chas Roy-Chowdhury, from the Association of Certified Chartered Accountants, put it:

> "We do not think it is simplification. We think if the £1,000 allowance or exemption was across the board rather than across different tax rates, that would be simplification. As it stands currently, the basic rate taxpayer has a £1,000 exemption, the 40% taxpayer has £500 and the 45% taxpayer has nothing. We think the cliff edge effect is unnecessary and is going to cause complexity."[32]

39. In his evidence Mr Williamson, from the Low Incomes Tax Reform Group, elaborated on the cliff edges:

> "You get very high marginal rates of course at the point where you become a higher rate taxpayer. At an income level of £43,000 you get a savings allowance of £1,000 and at £43,001 you get £500, so that is a marginal rate of tax of 500-odd per cent."[33]

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28 Q 64 (John Whiting); Written evidence from EY (FBB0018)
29 Q 5 (John Cullinane)
30 Q 80 (Cerys MacDonald)
31 Q 80 (Cerys MacDonald)
32 Q 1 (Chas Roy-Chowdhury)
33 Q 27 (Robin Williamson)

40. When it came to handling these complexities there was an obvious divide between those who could afford to employ an adviser and those who could not or chose not to. Keith Richards, representing the Personal Finance Society, felt that,

> "most typical IFA clients will already be fully cognisant with their tax position and therefore the changes will be less likely to have a significant material impact, other than perhaps in considering future investment strategies."[34]

41. Dermot Callinan, UK Head of Private Client at KPMG, went on to comment that his concern rested more, "with those on the margins—those who are perhaps not sufficiently wealthy to enjoy the services of an accountant or a personal adviser but are sufficiently wealthy to exceed the thresholds laid down by the Government."[35]

Lack of consultation

42. Whilst recognising that some of the design complexity may have resulted from Exchequer constraints, many felt that it could have been reduced by consultation in the early stages of the design of the Personal Savings Allowance as the new approach to tax policy-making requires. As reported in paragraphs 22 and 23 above, there had been a consultation on the abolition of the TDSI in July 2015. However, the Chartered Institute of Taxation pointed out that during that consultation HMRC,

> "had not announced how the saving allowance would work, so we were unclear about whether it would be a tax-free allowance or whether it would operate within the basic rate and higher rate bands. Ideally the consultation would have identified how the allowance would work, and we could have explained the unnecessary complexity and demonstrated the 'cliff edge' tax liabilities for taxpayers whose income levels fall just over the higher-rate threshold."[36]

43. On a more positive note, early publication of the draft Finance Bill is part of the consultative process, and this enabled the Association of Tax Technicians[37] and the Chartered Institute of Taxation[38] to identify an ambiguity in the drafting of a subsection of Clause 1 which inserts a new section 12A into Income Tax Act 2007. This subsection fails to make it clear that an individual who has savings income below £5,000 is entitled to the savings nil rate. In his oral evidence, Mr Brian Redford, from HMRC, agreed to consider putting the point beyond doubt.[39]

Implementation issues

44. The Government recognised that the abolition of the TDSI will involve initial costs for deposit takers in making systems and other changes and communicating with taxpayers, but expected them to experience savings later from not having to operate the scheme. It has not provided estimates of

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34 Q 49 (Keith Richards)
35 Q 50 (Dermot Callinan)
36 Written evidence from the Chartered Institute of Taxation (FBB0003). Mr Sanger from EY made a similar points (Q 67)
37 Written evidence from the Association of Taxation Technicians (savings) (FBB0002)
38 Written evidence from the Chartered Institute of Taxation (FBB0003)
39 Q 89 (Brian Redford), Q 90 (Brian Redford)

these initial costs but promised further details later this year.[40] Meanwhile, in evidence submitted to this inquiry, the Building Societies Association reported that, taking into account both system changes and customer communications, the "estimated cost to implement the TDSI changes range from around £3–£3.5 million for each of the larger societies down to tens of thousands for each of the smaller members."[41] They expected operational costs of the larger societies to fall over time by £150,000–£180,000 per year as compared with tens of thousands for the smaller ones.

45. The British Bankers' Association wrote that, although their industry was generally supportive of the changes introduced, "there is growing concern that the pace and scope of reforms are, at least in the short term, adding additional complexity for customers. In particular, the ongoing pace of changes may lead to an increase in uncertainty around tax rules which apply to savers."[42] They went on to encourage the Government to avoid further such changes during the lifetime of this Parliament to "allow time for those changes to settle and be understood by all customers."[43]

IT issues

46. There was no suggestion that any institution would not be in a position to implement the changes when they came into force in April. Commenting on the removal of TDSI, Sue Martin, of Lloyds Banking Group, said that:

> "Because they are big changes, a longer lead-in time is always better, but once we know when the changes have to be implemented, we obviously work with our people who need to be involved—the IT people—to make sure that we meet the deadline."[44]

Data matching

47. There were some concerns expressed about the extent to which HMRC would be able to attribute information received from financial institutions to the right taxpayer account when attempting to collect tax due. On behalf of TaxAid, Caroline Miskin's concern was with,

> "the accuracy of the data feed from the banks and HMRC's ability to link it up. With ISAs, the banks hold national insurance numbers and that is part of the feed of information to HMRC. It is a more difficult task for HMRC to match up data for other savers. In particular there might be joint accounts, trust accounts, that sort of thing."[45]

48. The British Bankers' Association added: "Implementation experience suggests that whenever existing data is used for new purposes, it should not be assumed that the implementation will be simple."[46]

49. On behalf of HMRC, Emma Churchill recognised the importance of accurate data matching and provided some reassurance:

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40 HMRC, *Income Tax: Personal Savings Allowance*, 9 December 2015: https://www.gov.uk/government/publications/income-tax-personal-savings-allowance/income-tax-personal-savings-allowance#contents [accessed February 2016]
41 Written evidence from the Building Societies Association (FBB0015)
42 Written evidence from the British Bankers' Association (FBB0005)
43 Written evidence from the British Bankers' Association (FBB0005)
44 Q 40 (Sue Martin)
45 Q 25
46 Written evidence from the British Bankers' Association (FBB0005)

> "In terms of the level of confidence we have about the information that is already coming to us from banks and building societies, as you would expect, we have been doing a series of test matches in our data systems. At the moment the level of accuracy is high, in the mid 90 percentage points. Of course that is not 100%, and we will be talking to the banks and building societies about whether there is anything we can do to increase it right up to 100% matching."[47]

Communicating with savers

50. One thread that ran through all the written and oral evidence submitted concerned the lack of awareness of taxpayers of their tax obligations under the current system and still less of the changes to come. In its written evidence[48] to the inquiry HMRC cited research[49] carried out for it on taxpayer awareness of how bank and building society is taxed. This found, among other things, that "customer understanding in this area is low", and that "many higher rate taxpayers are not aware of the requirement to account for additional tax, after the TDSI deduction by their bank or building society".[50] The OTS reported similar findings when it looked at pensioner awareness of the starting rate for savings income.[51]

51. Various witnesses[52] elaborated on the risks attendant on this lack of awareness for taxpayers—failing to recognise and comply with tax obligations, as well as failing to take advantage of tax benefits in making savings and investment decisions—and for the Exchequer after the abolition of TDSI.

52. Against this background, effective and timely communication with taxpayers potentially affected by these changes was seen as the key to their successful implementation, and to helping taxpayers make informed decisions about the most appropriate home for their savings. Mr Callinan, from KPMG, put it succinctly: "If the concern is awareness then the answer must be communication." He went on to say:

> "If we ourselves were running this as a business process, we would want to increase the amount of communication so that people could understand how it affected them. Complexity itself is not necessarily the problem; the problem is how you deal with it. If there is an adequate level of communication … complexity can be absorbed."[53]

53. Mr Richards, of the Personal Finance Society, commented that online communication tools were effective when people were already aware of an issue and where they were comfortable with the technology. He suggested that a number of communication mechanisms should be used:

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47 Q 86 (Emma Churchill)
48 Written evidence from HM Treasury and HMRC (FBB0016)
49 IFF Research (prepared for HMRC), *Awareness and Understanding of Taxation of Savings Interest*, May 2015: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/445858/Research_Report_370_Awareness_and_Understanding_of_Taxation_of_Savings_Interest.pdf [accessed February 2016]
50 Written evidence from HM Treasury and HMRC (FBB0016)
51 Office of Tax Simplification, *Review of pensioners' taxation: Final report*, January 2013: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/198500/ots_final_review_pensioner_taxation_230113.pdf [accessed February 2016]
52 Q 2 (Chas Roy-Chowdhury), Q 8 (Frank Haskew)
53 Q 55 (Dermot Callinan)

> "Every individual should be written to with a simple guide to help them decide whether the change affects them and what they should be alert to, and there are a whole range of other things that industry can join in. A lot of this has to be driven by HMRC with key messages that are very consumer-centric and help to raise awareness, and which then drive people to the right sources if they need more information. You should never underestimate the challenge of getting the message out to a large number of people."[54]

54. The majority of our witnesses saw communications initiatives as starting with HMRC. The Building Societies Association commented that the "onus should not only rest with financial institutions to communicate these changes to their customers. Instead there should be a broader awareness campaign that lets those who exceed their Personal Savings Allowance know what will happen."[55] The British Bankers' Association called for "a higher profile role for HMRC in communicating the changing landscape for bank customers, savers and taxpayers."[56]

55. HMRC's approach, however, appears to rely largely on banks and building societies informing their customers about the changes and the existence of further information on the GOV.UK website.

56. Mr Redford, giving evidence on behalf of HMRC, set out their approach:

> "We do not have a plan at present to mail the whole customer population that might have tax on interest. Our preferred method is to do this through the point at which they generally interact with the system, which is through their bank or building society. There is now further information on the GOV.UK website, including guidance from HMRC that was produced on Budget Day to explain the changes that were being made. Further guidance went there this week."[57]

57. He went on to say that, with the help of the OTS, the Low Incomes Tax Reform Group and other commentators, HMRC had produced a three-page information leaflet for banks and building societies to make available in their branches shortly. HMRC will take stock in April and "if we start to receive many calls and contacts from people who are confused, it is absolutely right for the department to put more effort and energy into conveying that message more strongly."[58]

58. Challenged on the timing of these information initiatives, Mr Redford replied that HMRC's aim was decide when to "provide as much information as we think is appropriate so that it is not too early so that people forget … It should come just at the point when they are making their decisions for the coming tax year."[59] He defended HMRC's use of the Government's website as its main means of communicating with savers:

> "We get very high traffic through GOV.UK and the tax-related pages on that. We know that social media is becoming more and more used, so as a method of communication that ensures that up-to-date information

54 Q 55 (Keith Richards)
55 Written evidence from the Building Societies Association (FBB0015)
56 Written evidence from the British Bankers' Association (FBB0005)
57 Q 81 (Brian Redford)
58 Q 81 (Brian Redford)
59 Q 80 (Brian Redford)

is provided for the widest possible audience, it is a very good way of communicating."[60]

59. For their part, the financial institutions that gave evidence to the inquiry appear to be gearing up to prepare their customers for the change as best they can and consulting with HMRC on the nature and accuracy of their messages. Ms Martin reported that Lloyds Banking Group had a large programme in place to deliver the changes needed and that included educating staff so that they could understand the new rules and support their customers.

Conclusions

60. **The evidence we have heard leads us to conclude that the introduction of the Personal Savings Allowance and the abolition of the TDSI represent useful simplifications for a large number of savers on relatively low incomes. However, we share the concern expressed by witnesses that these changes also bring significant increases in the complexity and compliance burdens faced by over one million[61] higher income savers and particularly those whose incomes take them to the margins of income tax bands. Those affected may include, for example:**

- **pensioners whose savings produce sufficient interest to exceed the new allowance. Many will not know of their obligation to report this income to HMRC; and**

- **savers on the margins of the tax bands. A saver whose income increases from £43,000 to £43,001 will face an increased tax liability of £100.20 because their tax free allowance will drop from £1,000 to £500.**

61. **We agree with those witnesses who said that the degree of complexity associated with these changes might have been reduced had consultation taken place in the early stages of policy development.**

62. **We are very concerned to hear about the low levels of taxpayer awareness of the current system for taxing savings income and that relatively little has so far been done to publicise the changes that come into effect this April and to prepare savers for them. We are not convinced by HMRC's current plans for communicating those changes.**

Recommendations

63. **We strongly recommend that, as a matter of urgency, HMRC replace their current approach to communications with a comprehensive strategy to make taxpayers aware of the abolition of the TDSI and the introduction of the new Personal Savings Allowance and of recent changes to ISAs and to the starting rate for savings income. This strategy should include a public awareness campaign led by HMRC in partnership with banks, building societies and other financial institutions. Using a wide variety of media, including more**

60 Q 83 (Brian Redford)
61 HMRC, *Policy Paper, Income Tax: Personal Savings Allowance*, 9 December 2015: https://www.gov.uk/government/publications/income-tax-personal-savings-allowance/income-tax-personal-savings-allowance [accessed February 2016]

traditional approaches, it should aim to inform savers of both their tax obligations and the need to review their savings choices in the light of the changes.

64. **We also recommend that the Government review:**

    (a) **the drafting of new section 12A Income Tax Act 2007, introduced by draft Clause 1, so as to clarify its meaning; and**

    (b) **its decision to retain a requirement to deduct income tax at source from some forms of savings income covered by the Personal Savings Allowance with a view to extending the coverage of the gross payment arrangements to other sources, if possible.**

CHAPTER 3: REFORMING DIVIDEND TAXATION

65. This chapter assesses the purpose and effect of the proposed changes to the taxation of dividends for individuals, comprising the abolition of the dividend tax credit, the introduction of the dividend allowance of £5,000 and the alteration in the dividend tax rates. These changes, which were announced in the Summer Budget 2015, are contained in draft Clauses 2 and 3 and the accompanying schedule.

66. The changes described above all take effect from 6 April 2016.

Taxation of dividends

The current position

67. Individuals who are UK resident taxpayers are taxed on dividends and other distributions from UK companies at dividend tax rates of 10% for basic rate taxpayers, 32.5% for higher rate and 37.5% for additional rate, on the dividend received grossed up by 1/9th. Under the UK's partial imputation system, such dividends carry a dividend tax credit of 10%. Dividend tax credits cannot be reclaimed by those whose income is below their personal allowance level or who benefit from other tax reliefs.

68. There is little understanding of the process of grossing up and tax credit calculations amongst taxpayers. Most simply consider the effective tax rate which, combining the dividend tax rate and the dividend tax credit, is 0% for basic rate taxpayers, so that all their income tax liability is met by the dividend tax credit. An effective tax charge of 25% of the dividend received is due from higher rate taxpayers and an effective tax charge of 30.56% from additional rate taxpayers.

69. Dividends received from investments held by individuals in ISAs are tax free but the tax credits cannot be reclaimed.

The history of grossing up and the dividend tax credit

70. The arithmetic grossing up of dividends received before applying a tax rate, then applying the dividend tax credit, derives from the imputation system, originally adopted in 1973 in order to provide relief from double taxation on distributed profits. The imputation system was substantially reformed in 1999 when the rate of corporation tax was reduced to 30%. While the dividend tax credit remained at a reduced level, it was no longer repayable to individuals. Corporation tax rates have been reduced further in recent years, to 20% in 2015, and the Chancellor has announced that he aims to cut the rate to 18% in 2020.[62] The economic justification for retaining the tax credit at its current value has therefore reduced with the rate of corporation tax.

Taxpayer behaviour in the current system

71. The extent to which individual taxpayers need to understand and engage with this system of dividend tax depends on their taxable income and their reasons for investing in a company. Investors with taxable incomes below the higher rate threshold do not need to consider their tax position as no liability is due and no dividend tax credit refund is available. Investors taxable at

62 HM Treasury, *Summer Budget 2015*, July 2015, p 3: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/443300/50325_HMT_Red_Book_Complete.pdf [accessed February 2016]

higher and additional tax rates should pay any additional tax due through the Self Assessment system or PAYE.

Minimising tax and National Insurance Contributions liabilities

72. Individuals who hold shares in private companies, particularly those actively involved in running the company, have more reason to engage with the system. They can determine whether the company pays its profits out to directors/shareholders as dividends or as salary. Salary payments are taxed at the basic, higher or additional rates of income tax (20%, 40%, 45%) as appropriate and generate a liability to employers' and employees' National Insurance contributions, of up to 13.8% and 12% respectively. A payment in the form of salary can frequently result in a combined income tax and employees' National Insurance contributions liability greater than the combined corporation and income tax liability of the same payment in the form of dividends. This difference in tax liabilities means that it has become routine for many private companies, including personal service companies, to adopt the form of pay-out which would minimise their overall tax cost. This is known as 'tax minimising profit extraction'.

73. Self-employed individuals face similar opportunities to the directors of private companies. They too can pay more tax and employees' National Insurance contributions than they would if they were to incorporate and pay dividends, again mainly due to higher employees' National Insurance contributions. Consequently, many self-employed individuals choose to set up and operate through a company, a process known as a 'tax motivated incorporation', although there are also a number of important commercial and legal reasons for incorporating, regardless of the tax position.

Countering taxpayer behaviour

74. UK tax legislation has few effective restrictions on the choice of business entity, whether made for commercial or tax reasons, other than in the relatively limited circumstances where the 'IR35' legislation applies in which case the individual is taxed broadly as if an employee of the engaging organisation. Non compliance with the IR35 regime is estimated to cost over £400m a year[63] and is again under review by the Government.

75. The Office of Tax Simplification (OTS) undertook a review of small business taxation in 2011 and suggested amendments to the 'IR35' procedure and the integration of income tax and National Insurance contributions to address the causes of the differences in liabilities. The House of Lords Select Committee on Personal Service Companies reported in March 2014 on the same issues, recommending a number of different actions to address the tax aspects of personal service companies.[64] Neither set of recommendations was fully implemented by Government, although the OTS is currently undertaking a project on the closer alignment of income tax and employees' National Insurance contributions.[65]For the moment the differences in tax and employees' National Insurance contributions treatments remain, and

63 HM Treasury, *Summer Budget 2015*, para 1.180: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/443300/50325_HMT_Red_Book_Complete.pdf [accessed February 2016].

64 Select Committee on Personal Service Companies, Personal Service Companies, (1st Report, Session 2013–2014, HL Paper 160)

65 Office of Tax Simplification, *Alignment of Income Tax and National Insurance, Terms of Reference*, July 2015: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/447209/ToR_closer_alignment_of_IT_-_NICs_review.pdf [accessed February 2016]

tax motivated incorporations and tax minimising profit extraction from small companies continues.

76. The draft Finance Bill 2016 proposes major reforms to the current system of dividend taxation with effect from 2016/17. These reforms are driven to a large extent by the need to stem the loss to the Exchequer from tax motivated incorporations and tax minimising profit extraction.

The draft legislation

77. Clause 3 and the accompanying schedule abolish the dividend tax credit and with it a number of legislative provisions left over from the partial imputation system.

78. Clause 2 introduces the new dividend allowance, a rather confusing description as in legislative terms it is a 'dividend nil rate' band on the first £5,000 of dividend income received by an individual, inserted into section 6(3)(b) Income Tax Act 2007.

79. Clause 2 also introduces a new section 13A into Income Tax Act 2007, to give effect to the new dividend tax rates on dividend income above £5,000. The Chancellor has announced[66] these will be 7.5% for basic rate taxpayers, 32.5% for higher rate taxpayers and 38.1% for additional rate taxpayers although these rates do not feature in the draft clauses released so far.

80. Section 13A also provides a mechanism to ensure that the £5,000 allowance has to sit within the existing basic and higher rate tax bands. As with the Personal Savings Allowance, whilst no tax is paid on the £5,000 dividend income, that income is still included in the definitions of taxable income. Unlike the Personal Savings Allowance, the dividend allowance is the same for all taxpayers regardless of their marginal rate.

81. The schedule to Clause 3, paragraphs 31 to 34, amend sections 1100–1106 of Corporation Tax Act 2010. These retain the obligation on a company to send a shareholder a tax certificate (dividend voucher) after making a dividend payment, but the tax certificate must no longer show a tax credit.

Effect of the reforms

82. The Government expects that the £5,000 dividend allowance will mean that more than 75% of taxpayers who receive dividend income will pay either less or the same amount of tax on their dividends. Those who will pay the same tax are primarily basic rate taxpayers with dividends of less than £5,000. Those who gain are primarily higher and additional rate taxpayers with dividends of less than £5,000, who could save a maximum £377 each.

83. A quarter of dividend recipients will pay more tax. They include 200,000 basic rate taxpayers with dividend income over £5,000 who would previously have had their tax liabilities fully offset by the tax credit. These may be investors as well as those who have minimised their tax liabilities by paying themselves dividends rather than salaries. The Low Incomes Tax Reform Group commented:

66 HM Treasury, *Summer Budget 2015*, July 2015 para 1.188: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/443300/50325_HMT_Red_Book_Complete.pdf [accessed February 2016]

"The abolition of the dividend tax credit will for the first time expose any basic rate taxpayer with dividend income of over £5,000 to a tax liability on their dividend income above that amount. There could also be unwelcome effects on low paid workers the engagers of whose labour require them to work through personal service companies."[67]

84. Those who pay tax at the higher or additional rate and have dividend income exceeding £5,000 will pay more tax. Higher rate taxpayers will see a reduced benefit from profit extraction by dividend rather than salary, but much depends on the exact circumstances and some anomalies arise. Additional rate taxpayers will face much higher tax costs, broadly removing much of the economic benefit they would have had from payment of dividend instead of salary.

85. The total Exchequer impact of the combined dividend tax changes for 2016/17 is estimated at £2.54bn, including £190m from a reduction in the number of new business incorporations. Over the period to 2020/21 the total impact of these changes is to increase Exchequer receipts by £8.85bn, including £2.06bn from new businesses not incorporating when they might otherwise have done so. [68]

Other objectives of the dividend tax reform

86. As well as reducing the tax incentives outlined above, the Government considers that these reforms will modernise the tax system by abolishing dividend tax credits, which are increasingly difficult to justify at their current level. They could also deliver some useful simplifications by removing the need for individual taxpayers to understand dividend tax credits. This inquiry has focussed on the extent to which this simplification benefits taxpayers and reduces compliance burdens, rather than on the effectiveness of the reforms in addressing the issues of tax motivated incorporation and tax minimising profit extraction.

Simplification

87. Simplification for taxpayers comes from the removal of the dividend tax credit, making it easier for taxpayers to understand the way dividends are taxed. For those who did actively consider their tax position, they will no longer need to consider the meaning of the tax credit on a dividend voucher, or whether it is repayable, nor the complexity of the tax credit calculation or differences between dividend tax rates and effective tax rates.

88. HMRC's evidence stated that they "frequently receive questions from people who often misunderstand the complex rules and the reason for the credit being non-payable."[69] John Whiting, of the OTS, said:

"I would add that it is a simplifying measure in that a lot of people will no longer have to worry about tax on dividends. Then again, they did not anyway in most cases. The simplification in some ways is more subtle because they will understand it better … this is getting to a simpler, more understandable system."[70]

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67 Written evidence from the Low Incomes Tax Reform Group (FBB0011)

68 HM Government, *Summer Budget 2015: policy costings*, July 2015, p 20: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/443195/Policy_costings_summer_budget_2015.pdf [accessed February 2016]

69 Written evidence from HM Treasury and HMRC (FBB0016))

70 Q 65 (John Whiting)

89. As with the changes to the taxation of savings income, the benefits of administrative simplification go principally to taxpayers being taken out of tax because their dividend income falls below the £5,000 dividend allowance. For those with dividend income greater than £5,000, the system is more complex and the overall perception of simplification a lot less clear. This was a consistent theme from our witnesses, summed up by Caroline Miskin of TaxAid who said: "I think the £5,000 dividend allowance was an attempt to mitigate the additional complexity of these rules for a significant group of taxpayers who have dividends of less than £5,000."[71]

Compliance burdens

Individual investors

90. Whether the fact that the new system is easier to understand than the old leads to reduced complexity and compliance burdens is a less straightforward question. Increasingly the income tax system is being fragmented into separate parts or sub-systems covering, for example, savings income, dividends, child benefit, ISAs, married persons and civil partners, pensions—each with their own allowances or nil rate bands. As a result it is sometimes the case that a change designed to simplify one part of the tax system produces greater complexity elsewhere. Thus it is possible to simplify any one component while making the whole system much more complicated. Basic rate taxpayers whose dividend income is below £5,000 avoid the complexities of the dividend tax credit system as noted above. However those close to the limit will have the increased compliance burden of having to monitor that their dividend levels do not rise over £5,000, which was not previously a relevant limit in the tax system.

91. HMRC estimates that only 8,500 basic rate taxpayers at present have dividend income above the £5,000 dividend allowance level.[72] Nonetheless, they will have a new obligation to notify HMRC of their dividends and take active steps to settle their tax liability in 2016/17, whether by PAYE or Self Assessment. This may be relatively simple, but the monitoring of income against the £5,000 dividend level will be an annual task. [73]

92. The Chartered Institute of Taxation and the Low Incomes Tax Reform Group also identified issues for taxpayers who make charitable donations under Gift Aid, noting that,

> "the combined effect of the savings allowance, the dividend allowance and the removal of the requirement for banks and building societies to deduct basic rate income tax at source from interest payments, may mean that they no longer pay sufficient tax to cover the tax attributable to their gift aid donations, and would be liable for the shortfall."[74]

93. It is becoming more difficult for individuals other than basic rate taxpayers to manage their own tax affairs without having to incur the costs of professional advice.

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71 Q 29 (Caroline Miskin)

72 HMRC, *Income Tax: changes to dividend taxation, policy paper*, December 2015: https://www.gov.uk/government/publications/income-tax-changes-to-dividend-taxation/income-tax-changes-to-dividend-taxation [accessed February 2016]

73 Written evidence from the Association of Tax Technicians (Dividend rate) (FBB0009)

74 Written evidence from the Chartered Institute of Taxation (FBB0003); Written evidence from the Low Incomes Tax Reform Group (FBB0011)

Director/shareholders of small companies

94. Frank Haskew, from the Institute of Chartered Accountants in England and Wales, suggested that it was very difficult for higher rate taxpayers in small companies and their advisers to understand how the rules impacted their tax positions:

> "We have had some examples of how the dividend rules … are working … When you look at them, you will see that they are incredibly difficult for people to understand. We struggle as tax practitioners with this. We have had quite a lot of arguments about how the rules work. If we are having trouble with it, I think it is going to be very difficult for the ordinary citizen to understand how their tax is being calculated."[75]

Interactions

95. Evidence was also presented that higher and additional rate taxpayers would face greater complexity in their tax affairs, particularly when considering the interaction of the dividend allowance with the Personal Savings Allowance and other allowances based on income. Deloitte commented specifically on the interaction with the high income child benefit charge and the restriction of the personal allowance which are based on whether 'adjusted net income' exceeds £50,000 or £100,000 respectively. Deloitte highlighted that income within the personal savings allowance and dividend allowance will count towards the definition of adjusted net income. Deloitte commented that:

> "In all cases the inclusion of the income somewhat dilutes the effect of what was introduced as an exemption, but also adds considerable complexity to the affairs of those who are affected. This will be particularly relevant for those in receipt of child benefit who need to consider whether or not to claim it."[76]

96. As with the Personal Savings Allowance, trusts and personal representatives will not be entitled to the dividend allowance and so will face additional complexity. The Association of Taxation Technicians considered that their additional administrative burden needs further consideration by HMRC.[77]

Personal financial decisions

97. Higher and additional rate taxpayers are also likely to need to review their savings portfolios to take into account changes to different tax reliefs and exemptions and their implications for different investment strategies. For those not taking expert advice, Paul Johnson, of the Institute for Fiscal Studies commented: "I suspect there will be a lot of uncertainty about how this impacts."[78]

98. Keith Richards, of the Personal Finance Society, noted:

> "Generally the feedback is that there is a general lack of understanding of what has been announced or what that will be. In many ways the services

75 Q 3 (Frank Haskew); Crunch Accounting told the Sub-Committee: "A limited company director paying themselves primarily through dividends would be paying £1,528 more tax a year when their pre-tax profits are £48,000, whereas a director with £78,000 pre-tax profits will only be paying £1,343 more tax". Written evidence from Crunch Accounting (FBB0001).

76 Written evidence from Deloitte LLP (FBB0004)

77 Written evidence from the Association of Taxation Technicians (dividend rate) (FBB0009)

78 Q 17 (Paul Johnson)

> of our members are increasingly in demand at times like this to ensure the transition is as smooth as possible or that clients fully understand the implications for them. I am not entirely sure that simplification works as well for people who are unadvised at present."[79]

99. The Committee heard from witnesses, including Ms Miskin, from TaxAid, and Mr Johnson, from the Institute for Fiscal Studies, that for certain individuals, the combined effect of the Personal Savings Allowance and dividend allowance was that ISAs no longer carried a financial advantage and could involve higher costs than non-ISA savings.[80] We note that, responsibility for communicating to savers the need to take account of recent tax changes in making savings and investment decisions appears to be left entirely to the financial services industry, with little guidance from HMRC.

Multiple objectives

100. As was mentioned earlier, the dividend tax reform serves two main objectives: firstly, to counter existing incentives to incorporate and draw profits as dividends, and secondly, to modernise the taxation of dividends by removing the last vestiges of the imputation system, producing a simpler, more readily understood, method of taxing dividend income. Whilst they recognised the need to address both objectives, a number of witnesses attributed the resulting complexities to the attempt to find one policy measure that dealt with both objectives. Speaking on behalf of the Chartered Institute of Taxation, John Cullinane accepted that for those whose dividends were taken out of tax altogether the system was simpler, but,

> "on the other side, for people who either control or together with a number of other people control a company, the Government clearly wanted a rough-and-ready way to get closer to a position where, whether people were sole traders or had companies and took the dividends out, they were paying something more comparable overall. I can see a simplification argument for the broad concept. However, they have not introduced those two regimes by trying to distinguish between the portfolio shares and the ownership shares. They have done it by saying it is £5,000."[81]

101. Mr Cullinane went on to suggest that the measure should have been more focused on close companies[82] and a withholding tax for dividends they paid might have provided a simpler way of achieving the same overall effects.[83] Chris Sanger, of EY, commented in similar terms:

> "There is still an incentive to incorporate, so it has not gone the whole way. You could have made that more targeted. If your concern was tax motivated incorporation alone, you could have chosen to focus on the close companies—so those with five or fewer participants—rather than imposing this as a burden on everybody. This has two different objectives, which have been blended together and not necessarily in the simplest manner."[84]

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79 Q 49 (Keith Richards)
80 Q 29 (Caroline Miskin) and Q 17 (Paul Johnson)
81 Q 6 (John Cullinane)
82 Broadly, companies controlled by five or fewer participators (shareholders).
83 Q 6 (John Cullinane)
84 Q 55 (Chris Sanger)

102. In their written evidence, EY also suggested that an approach that aligned dividend tax rates with income tax rates but kept the dividend tax credit would have avoided the complexity arising from a proliferation of tax rates.[85]

103. Mr Whiting, of the OTS among others, acknowledged the trade-offs in addressing the objectives simultaneously: "I am still not sure what the real driver is here. Is it simplification, in which case, yes, it has some gains, or is it taxing the tax motivated incorporation, in which case I would have liked to have thought about whether this was the simplest way of doing that?"[86]

104. Professor Judith Freedman, of the Said Business School, University of Oxford, also questioned the means adopted to resolve the trade-off. She referred to the Mirrlees review proposals which also recommended increasing the tax on certain dividends,[87] but she thought the Government's approach was "achieving a kind of simplification in such a very messy way that you cannot really see that is what is being achieved."[88]

105. As was the case with the evidence on the introduction of the Personal Savings Allowance, several witnesses argued that, because there was no clear statement of the Government's strategy for taxing savings and investment, those with higher dividend income could find their choices distorted in unintended ways. Mr Johnson, of the Institute of Fiscal Studies, noted: "I suppose one worry that I have is that the unintended consequence of putting all these things together is that owner-occupied housing looks increasingly like the best bet from a tax point of view and, therefore, the price of that is pushed further."[89]

Lack of consultation

106. Several witnesses considered that these complexities could have been addressed, and perhaps alleviated, had the Government engaged in a consultation process over the summer of 2015 on the policy and detailed design proposals. Mr Cullinane, of the Chartered Institute of Taxation, said: "The source of the problem is this continual piling on of complexity … often without any consultation. Often the most complicated things that come out are the ones without any prior consultation."[90]

107. The Federation of Small Businesses was also concerned about the absence of proper consultation: "While we can understand the rationale for addressing the long recognised imbalance in the tax system due to the tax treatment of dividends … this has caused substantial disquiet among FSB members."[91] Mike Cherry, representing the Federation, commented: "Our problem is with the way the announcement came through. There has been no consultation by the Government on this significant change."[92]

108. It appears that HMRC and HM Treasury did not take the opportunity either to inform taxpayers and their representative bodies of the rationale of the Government's decisions, or to consider whether simpler, better outcomes

85 Written evidence from EY (FBB0018)
86 Q 65 (John Whiting)
87 James Mirrless, Stuart Adam et al, *Tax by Design,* (Oxford University Press, 2011)
88 Q 23(Prof Freedman)
89 Q 17 (Paul Johnson)
90 Q 14 (John Cullinane)
91 Written evidence from the Federation of Small Businesses (FBB0007)
92 Q 70 (Mike Cherry)

might have been found. We are disappointed that public consultation was not undertaken—particularly important in the case of tax changes as significant as these—as the Tax Consultation Framework requires.

HMRC's communication strategy should be reconsidered

109. We understood from witnesses that the publication of the HMRC "Dividend Allowance Factsheet"[93] in August was HMRC's principal method of clarifying the proposals. Unfortunately, it soon became clear that it fell short of explaining the complexity facing many taxpayers and the Institute of Chartered Accountants of England and Wales attempted to shed light on the proposals in a paper referred to by Dermott Callinan, of KPMG, and written by Rebecca Benneyworth (former Chair of the Tax Faculty at the Institute of Chartered Accountants in England and Wales).[94]

110. Speaking on behalf of HMRC, Brian Redford confirmed the limited nature of HMRC's communications about the dividend changes to taxpayers. He contrasted the position of these changes with those affecting savings income where the TDSI is operated by a relatively small number of banks and building societies rather than a vast range of companies who pay dividends. As a result, HMRC,

> "do not have the same ability to say 'Would you do this with all your customers?' To that extent, we have not engaged with them to ask them to communicate; our messaging has been via the Government website and will be reflected in our self-assessment products, which will show the different allowances."[95]

111. It is not clear to us why, if HMRC's research shows that taxpayers are unclear about their reporting obligations for savings interest,[96] they should be any clearer about their reporting obligations for dividends without a comprehensive communications exercise by HMRC. Mr Redford suggested that the scale of the problem was limited: HMRC estimated only around 8,500 taxpayers would need to notify dividend income to them for the first time so that tax could be collected through Self Assessment or PAYE. The HMRC estimate assumes that all those with dividends over £10,000 are already in Self Assessment.[97] Emma Churchill, also from HMRC, informed us that Simple Assessments automatically reflecting dividend income are some years away.[98]

Clarity on corporate obligations

112. There is a general lack of understanding that the draft legislation provides that companies paying dividends would continue to issue dividend vouchers to shareholders but these would no longer show tax credits. Sue Martin,

93 HMRC, *Dividend Allowance Factsheet* August 2015: https://www.gov.uk/government/publications/dividend-allowance-factsheet/dividend-allowance-factsheet [accessed February 2016]

94 Q 52 (Dermot Callinan); Rebecca Benneyworth, *Dividend Taxation, 2016 and beyond,* version 2, August 2015: http://www.ion.icaew.com/TaxFaculty/post/Taxation-of-dividends-B602EE11FE8F4050B43D48D398696195 [accessed February 2016]

95 Q 82 (Brian Redford)

96 IFF Research (prepared for HMRC), *Awareness and Understanding of Taxation of Savings Interest,* , May 2015: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/445858/Research_Report_370_Awareness_and_Understanding_of_Taxation_of_Savings_Interest.pdf [accessed February 2016]

97 Q 87 (Brian Redford)

98 Q 87 (Emma Churchill)

from Lloyds Banking Group, understood this to be a matter of choice[99] and Grace Stevens, from Legal and General, suggested that the format of the information provided to shareholders on dividends might change.[100] Mr Redford from HMRC confirmed that companies' obligations were not changing to require them to report dividend payments to HMRC under these proposals.[101] He indicated HMRC might undertake research later this year to establish the need for further communications, if they get a significant volume of calls enquiring about the changes.[102]

Conclusions

113. **Although witnesses agreed that taxpayers with relatively small portfolios will eventually find the new dividend allowance and abolition of dividend tax credits easier to understand than the present system, there were concerns about the added complexity for savers with larger portfolios and for small company directors/shareholders and about the absence of consultation on these proposals.**

114. **We share those concerns and agree that some of the complexity might have been avoided had there been early consultation in accordance with the Tax Consultation Framework.**

115. **We are also concerned that HMRC may not have fully appreciated the need for clear and timely communication to taxpayers so that they can continue to make informed personal financial decisions, and meet their obligations, and that companies have not been informed of HMRC's plans for making shareholders aware of the changes.**

116. **We are not convinced that HMRC's plans to put information on GOV.UK are sufficient to raise the awareness of taxpayers to their new responsibilities without the help of companies paying dividends.**

Recommendations

117. **We recommend that HMRC urgently develop a comprehensive communications strategy to make taxpayers aware of the changes. In particular taxpayers should be informed:**

(a) **what the dividend tax changes mean for them in making appropriate financial decisions, including their impact on ISA savings; and**

(b) **how they should use the information they receive from companies to complete their tax returns or check tax assessments they receive from HMRC.**

99 Q 41 (Sue Martin)
100 Q 44 (Grace Stevens)
101 Q 82 (Brian Redford)
102 Q 82 (Brian Redford)

CHAPTER 4: SIMPLE ASSESSMENT AND MAKING TAX DIGITAL

118. This chapter considers draft Clause 71 which gives HMRC the power to assess an individual's income tax liability on the basis of information supplied by third parties, without that individual submitting a Self Assessment tax return. To place the clause in context, the chapter provides brief summaries of the current tax assessment and collection arrangements and of the role of Simple Assessments as the first step towards the implementation of the Government's plans for '*Making Tax Digital*' by 2020.[103]

119. The legislation introducing Simple Assessments will apply from 6 April 2016 and the first such assessments will be issued in respect of the 2016/17 tax year. HMRC expect to issue the first Simple Assessments in summer or autumn 2017. The other measures discussed in this chapter, including those leading to legislative proposals in the Finance Bill 2017, will be the subject of consultations over the coming months.

Current income tax collection arrangements

120. There are three main income tax collection mechanisms in the UK:

 (1) Pay As You Earn (PAYE)

 (2) Self Assessment

 (3) the TDSI and other schemes covering income tax on other savings and investment income such as dividends

121. The TDSI and the current system of dividend tax credits, discussed in Chapters 2 and 3 respectively, are both due to be abolished by the Finance Bill 2016.

Pay As You Earn

122. PAYE was introduced in 1944. It is a system whereby employers (and pension providers) are obliged to withhold, and pay over to HMRC, income tax and National Insurance contributions on the earnings of (and other payments to) their employees. The amount of tax and National Insurance contributions to deduct from an employee's wages or salary is calculated by the employer by applying a 'PAYE code' supplied by HMRC. This code is determined by HMRC on the basis of the allowances, reliefs and exemptions it expects the employee to be entitled to for the tax year. Tax due on the employee's income from other sources may also be reflected in their PAYE code.

123. The PAYE system was originally designed to collect the right amount of tax in a world in which nearly all employees had only one job and little, if any, other income, and job changes were relatively infrequent. As the work environment has changed over time, the PAYE system has struggled to cope and has undergone a series of reforms and adaptations.

124. The most recent, and arguably the most radical, reform to PAYE was the introduction of the 'real time information' system, whereby employers

103 HMRC, *Making tax easier: The end of the tax return'*, March 2015: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/413975/making-tax-easier.pdf [accessed February 2016]

are required to transmit (electronically) to HMRC information about their employees' pay and tax deducted at the same time as their net pay is transferred to their bank accounts. Real time information also has a central role to play in the 'pre-population' of tax returns (see paragraph 132 below) and, eventually, the determination of Universal Credit entitlements.

125. The rollout of the real time information system started in April 2013 and was completed in 2015 with the smallest employers being brought in, although there remain some minor exemptions. In April 2014 there were some 1.9 million PAYE schemes reporting through real time information.

Self Assessment

126. The Self Assessment system of tax assessment and collection was introduced in 1996/97 to cover (mainly) individuals whose tax affairs were not fully covered by PAYE and the various deduction at source schemes.

127. Under Self Assessment the responsibility for notifying tax liabilities and making accurate tax returns is clearly on the individual taxpayer and failure to do so is supported by a penalty regime. Self Assessment taxpayers must report their income from all sources, and claim any allowances and tax reliefs by completing a tax return and their tax bills are calculated on the basis of that information. HMRC then has set time limits within which it can carry out enquiries and challenge the accuracy and truthfulness of the taxpayer's return. HMRC uses the information it receives from employers, pension providers, banks and other institutions to check returns, but it does not currently use that data to partially complete ('pre-populate') individual taxpayers' returns in advance.

128. Individuals required to submit tax returns must do so by 31 October following the end of the tax year if they are submitting a paper return and by 31 January if they are completing their return online. 86% of tax returns are currently completed online rather than on paper.

129. Outstanding tax must be paid by 31 January following the end of the tax year and those whose tax liabilities are not largely covered by PAYE or deduction at source must also make two estimated 'payments on account' in respect of their following year's tax bill. Those who are eligible to, and wish to, have any outstanding tax collected through PAYE must submit their returns by 30 December.

130. Self Assessment tax returns must be completed by, broadly speaking, individuals who are self-employed, directors, have significant rental or investment income, untaxed foreign income or taxable capital gains, or whose tax affairs are relatively complicated, because, for example, they are affected by one of the cliff edges or tapers applying to certain tax reliefs (see Chapter 6, Box 1).

131. In spite of HMRC's efforts to deal with smaller outstanding tax liabilities outside the Self Assessment system by using Form P800 to make 'informal assessments' of tax liability and by other means, over 10 million people are currently required to submit tax returns, up from some 8 million in the late 1990s. This growth in the numbers falling within the Self Assessment net arises from a variety of factors including rising incomes, fiscal drag for higher rate taxpayers, changing employment patterns and the increasing complexity of the personal tax system.

Moving to 'digital tax accounts'

Background

132. Although HMRC receives income data from a variety of sources it has not so far used that information to assess tax liabilities routinely. The introduction of real time information and improved HMRC IT systems (which can correctly match income details to taxpayers) will enable all available income information relating to certain individuals to be brought together to form the basis for an assessment of their tax liability in a 'Simple Assessment'.

Simple Assessments

133. In contrast to a 'Self Assessment', described in paragraphs 126–131 above, a 'Simple Assessment' of an individual's tax liability will be one made by HMRC based purely on information provided to HMRC by third parties such as employers, pension providers, banks, building societies and other institutions.

134. The purpose of Simple Assessment is to "enable HMRC to issue a legally enforceable assessment to those individuals with straightforward tax affairs where HMRC already hold all the information needed to calculate their tax position without the need for them to complete a return."[104] The requirement to complete a Self Assessment tax return will continue for individuals "whose tax affairs are not straightforward or where HMRC does not have all the necessary information to calculate their tax liability."[105]

The Government's vision for 2020

135. The introduction of Simple Assessments is a first legislative step towards replacing tax returns with 'digital tax accounts' by 2020 and it is therefore difficult to consider them in isolation. That aspiration was first articulated in a document entitled '*Making tax easier: The end of the tax return'*, published alongside the March 2015 Budget and spelled out in further detail in '*Making Tax Digital'* in December 2015, along with time lines for public consultations during 2016 and for the introduction of the various proposed changes from 2017 to 2020.[106] Most of the legislation underpinning the new system is expected to be in the draft Finance Bill 2017.

136. Broadly speaking, the changes envisaged involve:

(1) showing information from employers, pension providers, banks, building societies and other third parties on an individual taxpayer's digital tax account, and enabling taxpayers to report additional income through that account as it arises;

(2) for those who still receive Self Assessment tax returns, pre-populating parts of the return with third party information held by HMRC;

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104 HMRC, *Explanatory Note—Clause 71 and Schedule: Simpler assessments*, December 2015, para 18: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/484307/Draft_explanatory_notes_clause_71.pdf [accessed February 2016]

105 Ibid, para 19

106 HMRC, *Making tax easier: The end of the tax return',* March 2015: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/413975/making-tax-easier.pdf [accessed February 2016]; HMRC, *Making Tax Digital,* December 2015: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/484668/making-tax-digital.pdf [accessed February 2016]

(3) making more frequent adjustments to PAYE codes to collect tax due promptly and enabling those taxpayers whose outstanding tax cannot be fully collected via PAYE to settle their tax liabilities as they appear on their digital tax accounts; and

(4) extending digital reporting of income and expenses to businesses, whether incorporated or self-employed, and most private landlords, and requiring them to update HMRC at least every quarter, using digital tools to keep records of their income and expenditure.

137. The Government suggests that, once implemented, these changes, taken together, would have the effect of making the Self Assessment tax return redundant.

The draft legislation

138. Clause 71 and its accompanying schedule essentially provide HMRC with the power to make Simple Assessments and demand the payment of the tax assessed to be due.

139. The Schedule amends Parts 2, 4 and 5 of the Taxes Management Act 1970 to:

(1) remove the requirement for an individual to notify HMRC of income that is subject to a Simple Assessment, while retaining an obligation to report any income or capital gains not included in the assessment (Paragraph 2)

(2) enable HMRC to withdraw a notice to file a tax return where it intends to make a Simple Assessment (Paragraph 4)

(3) provide for the introduction of Simple Assessments for individuals and trustees, setting out who qualifies, the basis of the assessment and the details that must be included on a Simple Assessment notice, including the information used and the amount due (Paragraph 5)

(4) allow HMRC to withdraw or suspend a Simple Assessment where an individual disputes it, normally within 30 days of issue (Paragraph 7)

(5) set out how the amount of tax due is calculated and when it should be paid, generally on or before 31 January after the end of the year of assessment (Paragraph 9)

140. The legislation will apply from 6 April 2016 so that the first Simple Assessments will be issued in respect of tax year 2016/17.

Simple Assessments and their implementation

141. Witnesses welcomed, in principle, the advent of Simple Assessment as a means of lightening the burden of collecting and accurately reporting to HMRC information HMRC already holds. John Whiting of the OTS commented that:

> "For HMRC to use information that it already has and use it to potentially pre-populate returns, rather than asking you or me to put

that information in again, process it again and potentially introduce errors, is going in wholly the right direction."[107]

142. The Chartered Institute of Taxation commented that, "In principle, the measures appear sensible and avoid the need to put taxpayers into self assessment."[108]

143. Organisations dealing with low-income taxpayers were particularly keen. The Low Incomes Tax Reform Group's evidence said:

> "We generally welcome this facility to assess individual taxpayers with straightforward affairs without putting them into self-assessment, particularly pensioners whose only taxable income is the state retirement pension (on which DWP will not operate PAYE), and others with insufficient PAYE income to enable collection of tax they owe."[109]

144. Caroline Miskin pointed out that her organisation TaxAid dealt with many such cases and commented that the fact that Simple Assessment "puts a stop to those two categories of people being issued with Self Assessments returns is a huge benefit to us."[110]

Taxpayer awareness

145. Echoing the issue of taxpayer awareness which emerged in Chapters 2 and 3, Deloitte wrote that:

> "Whilst this legislation is welcome in that it should simplify the tax affairs of those who are issued with simple assessments, there are areas of concern, mainly centering on the need for clear communication to affected taxpayers. Taxpayers must be made aware that the tax calculation in a Simple Assessment will be a legally enforceable demand for payment, which they will need to check carefully and take the necessary action within the 30 day time frame if they believe it to be incorrect."[111]

146. Deloitte also pointed to the risk that taxpayers would confuse Simple Assessments with "the annual reconciliation frequently issued to those taxed under PAYE, (P800) where typically any underpayment is recovered by changing the taxpayer's PAYE code."[112]

Checking Simple Assessments

147. On the need for taxpayers to check Simple Assessments, EY wrote that:

> "A key concern will be how to identify and resolve calculations based on incorrect, insufficient or incomplete information, all of which may lead to an inaccurate assessment … This will be particularly important for Capital Gains Tax liabilities, as it is unlikely that HMRC would have access to the information required to be able to accurately assess a person's liability."[113]

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107 Q 66 (John Whiting)
108 Written evidence from the Chartered Institute of Taxation (FBB0003)
109 Written evidence from the Low Incomes Tax Reform Group (FBB0011)
110 Q 31 (Caroline Miskin)
111 Written evidence from Deloitte LLP (FBB0004)
112 Written evidence from Deloitte LLP (FBB0004)
113 Written evidence from EY (FBB0018)

148. Some witnesses drew attention to the risk that, rather than meticulously checking their assessments, taxpayers would simply assume that they were correct because they came from HMRC and emphasised the need to make taxpayers aware of their changed responsibilities.[114]

149. On behalf of the Low Incomes Tax Reform Group, Robin Williamson saw as central the form in which HMRC presented the information: "The question of whether it is going to be easier for people to check will depend very much on how HMRC presents the information" and whether HMRC would draw attention to the taxpayer's entitlement to tax allowances and reliefs.[115] Emma Churchill from HMRC provided some reassurance on this point: "There may well be a summary at the end, but it is important that it is not only a summary that they receive … that we set out clearly exactly what information we have, from what source and how those pieces of information have been used to prepopulate and come up with a tax calculation."[116] We strongly agree.

150. HMRC officials told us that initially the third party information that Simple Assessments would be based on would consist mainly of employer and Department for Work and Pensions (DWP) information. Savings income data might be used if appropriate, but the nature of any company dividend data transmitted to HMRC was to be the subject of consultation later this year.[117]

151. There were some concerns about data quality and, particularly, DWP data. Ms Miskin of TaxAid told us that: "The worst offender is the data that comes from the DWP. The data on state pensions is by far the greatest source of inaccuracy on P800s."[118] The Low Incomes Tax Reform Group and others had similar concerns, and Mr Williamson advised that Tax Help for Older People's latest statistics show that 46% of the coding checks and 60% of the P800 checks they carry out reveal errors.[119]

152. Ms Miskin felt that it was unlikely that those receiving Simple Assessments would be able to check and challenge assessments within the 30 day window provided:

> "We are also concerned that there are only 30 days for individuals to dispute this with HMRC, which is a very short period. Typically, it is quite unusual for clients to come to us within 30 days of having received their tax bill from HMRC, because they worry about it for a while, try to phone HMRC, then maybe go to a front-line agency such as Citizen's Advice, and only then do they find us. It will be a real struggle for people to check these and be in a position to challenge them within 30 days."[120]

153. We share Ms Miskin's concerns and consider that, in deciding how long to allow taxpayers to dispute a Simple Assessment, the Government should bear in mind that many taxpayers will be unaware of the fundamental changes

114 Q 26 (Robin Williamson); Q 67 (John Whiting and Chris Sanger)
115 Q 31 (Robin Williamson)
116 Q 86 (Emma Churchill)
117 Q 87 (Emma Churchill)
118 Q 32 (Caroline Miskin); A P800 Form is used by HMRC to make 'informal assessments' of smaller outstanding tax liabilities outside the Self Assessment system.
119 Q 32 (Caroline Miskin) and Supplementary written evidence from the Low Incomes Tax Reform Group (FBB0014)
120 Q 31 (Caroline Miskin)

brought about by the abolition of the TDSI and of dividend tax credits and what those changes mean for the proper management of their tax affairs. Even for those taxpayers who are aware and understand these changes, 30 days is a relatively short time in which to gather the information required, sometimes from disparate sources, and check the accuracy of HMRC's assessment, and especially so in the first years after introduction.

154. Challenged on this point Ms Churchill of HMRC said that the 30-day time limit was "something that we have put out for consultation. The legislation is out for consultation and this is an area in which we have received a lot of responses, which of course we will take into consideration."[121]

Who will get a Simple Assessment?

155. There appeared to be some uncertainty as to exactly which taxpayer groups would receive Simple Assessments and why. Some commentators assumed that Simple Assessments would be used to collect tax on savings income which had previously been paid under deduction of tax. For example, Deloitte noted that: "As savings income will be paid gross from 6 April 2016 there will be an increasing number of people in this category."[122] Ms Miskin, of TaxAid, said that,

> "Part of the issue is that HMRC has not explained what it intends to use this power for. Informally, we know that it is intended for these PAYE underpayments and people claiming state pension, but HMRC has not made a public statement or put anything in writing as to exactly what it intends to use it for."[123]

156. HMRC's written evidence attempted to clarify the issue by saying that Simple Assessments would begin in 2016/17 for unrepresented individuals with the simplest affairs who would receive, instead of a tax return, "a simple tax calculation and a request for payment".[124] These would include "730,000 people who underpay through PAYE, and for whom HMRC cannot collect the difference through the next year's PAYE" and "17,700 pensioners whose state pension exceeds their personal allowance."[125]

Conclusions on Simple Assessment

157. **We commend the Government's plans to provide HMRC with the powers to make Simple Assessments of individuals' tax liabilities on the basis of third party information. They have the potential to reduce the compliance burdens imposed on low income taxpayers who are currently required to complete Self Assessment returns.**

158. **We share the concerns of witnesses about the need to ensure that the data used to make Simple Assessments is accurate and clearly presented in disaggregated form, so that each separate source of income is identifiable, and that those receiving such assessments are aware of their responsibility to check them carefully and dispute them if necessary. We are also concerned about the lack of public**

121 Q 87 (Emma Churchill)
122 Written evidence from Deloitte LLP (FBB0004)
123 Q 31 (Caroline Miskin)
124 Written evidence from HM Treasury and HMRC (FBB0016)
125 Written evidence from HM Treasury and HMRC (FBB0016)

information concerning HMRC's plans for rolling out the new assessments and for communicating the changes to taxpayer.

Recommendations on Simple Assessments

159. **We recommend, therefore, that HMRC take action to clarify and publicise: its plans for implementing the new assessments, the responsibilities of taxpayers receiving Simple Assessments and the information they can expect to receive from HMRC and third parties.**

160. **We are concerned by evidence that the information supplied to HMRC by the Department for Work and Pensions can be the cause of inaccuracies in the current system. Prior to the new arrangements being implemented, and DWP information being used to 'pre-populate' Simple Assessments, we recommend that HMRC take steps to satisfy itself that this data is robust and accurate.**

161. **In the light of the evidence submitted in response to the consultation on the draft Finance Bill 2016, we recommend that the Government review the requirement in the draft legislation to dispute a Simple Assessment within 30 days of its being issued. We are concerned that individuals will struggle to obtain, often from third parties, the information necessary to check their assessments and to dispute them within the time limit currently proposed.**

162. **We also recommend that HMRC produce and publish an analysis of the lessons to be learned from the first full tax year, 2016/17, in which Simple Assessments are implemented in good time to inform subsequent stages in the transition to digital tax accounts.**

The transition to digital tax accounts

163. Simple Assessments were presented as the first stage in the Government's plan to introduce digital tax accounts and the evidence submitted to the inquiry went wider than the immediate concerns of draft Clause 71. Whilst recognising that the Government intends to undertake extensive consultations in the course of this year on the implementation of its longer term plan, in the remainder of this chapter we present evidence pertinent to the development of the later stages of that plan and draw some conclusions which we think would help inform the coming consultations.

Support for the proposals

164. Most of our witnesses gave a guarded welcome to the general direction in which HMRC intended to travel and understood the drivers for change: of tightening resource budgets and rapid development and adoption of technological change. They were very uneasy about the pace of change, HMRC's ability to deliver the IT and other aspects of that change effectively, and the compliance burdens and risks involved for taxpayers, particularly those who were 'digitally excluded'.

165. Looking at the issue from a retail banking perspective, Sue Martin from Lloyds Banking Group was very positive: "Our research has shown that our customers feel that by having a digital account they feel more in control of

their finances. By extending that to a digital tax account they should feel in control of their tax as well."[126]

166. Chris Sanger, from EY, outlined some of the benefits for HMRC: "Digital taxation in this way offers two real benefits to HMRC. It offers it the ability to get a lot more data from sources … .It also allows it to provide a much better service to its customers, as it refers to taxpayers."[127] He warned, however, that if digitisation did not go hand in hand with simplification of the tax system, the Government risked "embedding the complexity that we have today into a computer system that will be very difficult to change."[128]

Concerns and areas for further consultation

167. The concerns witnesses raised about the proposals fell into three categories: implementation issues; support for taxpayers; and the requirements for quarterly, digital reporting by businesses.

Implementation issues

168. Mr Whiting, of the OTS, thought that the benefits of the change were clear but that people would need to be persuaded that the new system was "easy and not threatening. They just need to look and confirm and perhaps add one or two things. There will be a real hump to get over to get people switched on to this new way of doing things."[129] He went on to outline some of the challenges facing HMRC, including major IT systems changes and making sure that the information flows from third parties were accurate and properly matched to taxpayers' digital accounts. The Federation of Small Businesses wrote that "The accuracy of tax data is fundamental to the Government's '*Making Tax Digital*' agenda and lowering costs for taxpayers and business. Digital reporting is a mechanism that will only provide useful reports if the tax data is accurate."[130]

169. The Building Societies Association stated that it had "concerns about HMRC's ability to deliver this fundamental change"[131] but did not elaborate on them. The British Bankers' Association was more explicit about the data and IT challenges and urged,

> "early engagement between HMRC and all data providers to allow adequate time to implement and test changes. The scale and nature of these changes means that, to the extent that bank system changes are required, early visibility of requirements would be beneficial."[132]

170. On the issue of HMRC's having the resources to implement the move to digital accounts, Ms Churchill told us that it entailed a five-year programme and that,

> "the Chancellor's announcement in the spending review of £1.3 billion of investment in HMRC over the period specifically for the work that

126 Q 46 (Sue Martin)
127 Q 68 (Chris Sanger)
128 Q 68 (Chris Sanger)
129 Q 66 (John Whiting)
130 Written evidence from the Federation of Small Businesses (FBB0007)
131 Written evidence from the Building Societies Association (FBB0015)
132 Written evidence from the British Bankers' Association (FBB0005)

we need to do to make a reality of the vision that we have set out in the '*Making Tax Digital*' roadmap."[133]

Taxpayer support

171. The evidence we received suggested general concern about how taxpayers would be prepared for the move to digital accounts and supported during and after the move. They would need to be made aware of exactly what the changes meant for them individually and how they altered the balance of responsibilities between the taxpayer and HMRC and where they could go for help. Witnesses emphasised the need for wide-ranging education and awareness raising initiatives and information and support across a range of media.

172. A major area of concern was the ability of some taxpayers to engage with a system which, if it were eventually put in place, would increasingly rely on them accessing HMRC services, including guidance and taxpayer support, digitally. The Chartered Institute of Taxation summarised the issue well:

> "We also wonder whether HMRC's longer-term strategy in relation to customer service will be effective. This appears to focus on 'self-help' rather than HMRC help, and for that HMRC help to become increasingly digitalised (You Tube videos, online chat, etc) which might leave those who are uncomfortable with this kind of communication, or the digitally excluded, being unable to easily find help."[134]

173. It is estimated by HMRC that there are some 7 million adults in the UK who are termed 'digitally excluded', although not all of them are taxpayers. According to Mr Williamson (from the Low Incomes Tax Reform Group):

> "They include older people who never learned computers at school and who have not got used to them since; people with disabilities who find it difficult or painful to use computers or the internet … and people in remote areas … and there is no broadband connection."[135]

174. Speaking on behalf of the Federation of Small Businesses, Mike Cherry stressed that "there are still many companies, many individuals, who do things manually and are not even using software packages or simple spreadsheets."[136]

175. When we took evidence from HMRC officials, Ms Churchill assured us that HMRC had the problem in hand:

> "It is also important to say that we also have in our spending plans for HMRC the support that customers will need to make the transition to digital … We know that not all our customers will find the transition to digital easy, and that we will need to continue to invest in multichannel support, whether by phone or through our Needs Extra Support service."[137]

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133 Q 86 (Emma Churchill); HMRC, *Making Tax Digital*, December 2015: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/484668/making-tax-digital.pdf [accessed February 2016]

134 Written evidence from the Chartered Institute of Taxation (FBB0003)

135 Q 36 (Robin Williamson)

136 Q 72 (Mike Cherry)

137 Q 86 (Emma Churchill)

Digital record keeping and quarterly reporting

176. Perhaps the most controversial area was HMRC's proposal that most businesses, including the self-employed and private landlords, keep their business records in digital form and update their digital accounts quarterly.[138] Witnesses from the small business community expressed disquiet about this. Some see the proposals, if adopted, as a 'Trojan horse' disguising the implementation of a mandatory quarterly payment requirement which would damage businesses' established cash flows.[139]

177. The Federation of Small Businesses argued that such reporting would be disproportionately burdensome, and wrote that it was,

> "extremely concerned about proposals to introduce mandatory quarterly tax reporting for small businesses and the self-employed. While we support the voluntary use of digital reporting, we believe that quarterly reporting must not be mandatory for all businesses. Instead, it should be adopted as a matter of choice by firms that can benefit from real-time reporting as an effective management tool."[140]

178. Andrew Chamberlain of the Association of Independent Professionals and the Self-Employed and Mr Cherry from the Federation of Small Businesses voiced similar concerns, stressing that the new system will "come at a cost".[141] In addition to these significant compliance costs, Mr Chamberlain and Mr Cherry considered that there had not been a proper impact assessment of the proposal and, indeed, that too little public information had been released about the detail of the proposals. [142]

179. This concern is apparent not just from the evidence submitted to this inquiry, but also to other inquiries. In its report on the Spending Review and Autumn Statement 2015, the House of Commons Treasury Select Committee concluded that,

> "some elements of HMRC's Making Tax Digital plans, most notably the quarterly reporting requirement for all businesses, may create additional burdens for taxpayers. HMRC's discussion paper implies that it could even require them to pay tax before it is legally due. It is premature to make the case for these plans on the grounds of simplicity and convenience for taxpayers. The main benefits appear to arise largely from additional revenue to the Exchequer, partly at the expense of cash flow to businesses where they need to pay their tax earlier, and partly as a result of a reduction in the amount of errors. Much more consultation over the detail is required before this policy is implemented. Legitimate concerns of businesses about the burden that may be caused by this policy need to be addressed by HMRC and the Treasury."[143]

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138 HMRC have stated, "By 2020, most businesses, self-employed businesses and landlords will be required to keep track of their tax affairs digitally and update HMRC at least quarterly via their digital tax account. These changes will be introduced for some businesses from April 2018, and will be phased in by 2020, giving businesses time to adapt"; HMRC, *Making Tax Digital,* December 2015: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/484668/making-tax-digital.pdf [accessed February 2016]

139 Written evidence from the Federation of Small Businesses (FBB0007)

140 Written evidence from the Federation of Small Businesses (FBB0007)

141 Q 72 (Andrew Chamberlain)

142 Q 70 and (Mike Cherry and Andrew Chamberlain)

143 Treasury Committee, Spending Review and Autumn Statement,(Sixth Report, Session 2015–2016, HC Paper 638)

180. Ms Churchill, of HMRC, said that there had been a misunderstanding about the announcements in December and that HMRC were going to consult on the information that "businesses will be required to keep digitally, and the information they will be required to send us via a quarterly update, but that does not equate to four tax returns a year." She went on to stress that HMRC had,

> "announced that we will require businesses to keep that information digitally within software or applications that are then linked directly into our systems … The point about digital record-keeping is that it will reduce very significantly the errors that are made."[144]

181. Ms Churchill pointed out that the benefits did not go simply to the Exchequer. Digital record-keeping could enable businesses to be run and planned better, but she recognized that many small businesses would need support, including free software, during the transition.[145] Responding to concerns about the lack of a comprehensive impact assessment,[146] Ms Churchill said that there would be an initial assessment as part of the consultation in the spring and a fuller one when draft legislation was published in December.[147]

Conclusions on digital accounts

182. **We recognise that the Government will be undertaking consultations on the remaining features of the transition to digital tax accounts in the next few months and draft clauses will not be available for scrutiny until December when the draft Finance Bill 2017 is due to be published.**

183. **We found many of the issues raised in the evidence submitted concerning. Questions remain: how will elderly people who are not confident using online resources manage their tax affairs? How can rural businesses with poor broadband access meet their obligations under a digital system? We conclude that these measures require detailed consideration before policy decisions are taken and draft legislation is made available.**

Recommendations on digital accounts

184. **We commend the Government for publishing a comprehensive timetable for these consultations and we recommend that they include:**

(1) **a full assessment of the impact of the 'Making Tax Digital' proposals, including any new reporting requirements and compliance costs, on smaller businesses. This should address the significant concerns raised with us by business representatives, particularly the proposed quarterly reporting and the associated possibility of quarterly payments, and include any evidence to support the Government's claims that digital record keeping will yield business benefits;**

144 Q 84 (Emma Churchill)
145 Q 84 (Emma Churchill)
146 Written evidence from the Federation of Small Businesses (FBB0007)
147 Q 85 (Emma Churchill)

(2) **an analysis of any changes in the powers of HMRC and in the obligations of taxpayers as a consequence of the move to digital accounts; and**

(3) **a detailed outline of HMRC's plans to educate and support taxpayers, particularly those not acquainted with, or without access to, new technologies, through the transition to and in the early years of the new system.**

CHAPTER 5: THE ROLE OF THE OFFICE OF TAX SIMPLIFICATION

185. This chapter considers the proposals to put the Office of Tax Simplification (OTS) onto a statutory footing. It describes the current role and functions of the OTS and its work so far, before addressing the proposed changes announced in the Autumn Statement 2015 and published in the draft Finance Bill 2016 (Clauses 83–88 and the accompanying schedule).

Current role and functions of the OTS

186. The OTS was established in 2010 to provide independent advice to the Government on simplifying the UK tax system and on reducing tax compliance burdens for businesses and individual taxpayers. Its core duties were to:

- identify areas of complexity where the Government could simplify the tax system, and
- undertake detailed reviews of particular areas of tax law to identify options for reform.[148]

187. The OTS remit does not extend to tax policy design; rather its focus is on existing statutory complexities with areas of work decided on by the Chancellor. The OTS is purely advisory and the decisions on which recommendations to follow through, and how to give effect to them, remain with the Chancellor.

188. The OTS was initially set up on a temporary basis as an Independent Office of HM Treasury. Its role, responsibilities and governance were set out in an Interim Framework Agreement between the OTS, HM Treasury and HMRC. Detailed work has been under the control of the (part time) Tax Director with a small OTS staff, mainly seconded from the private sector, HMRC and HM Treasury, with expertise relevant to chosen projects.

189. In undertaking its projects, the OTS has carried out extensive public consultations and engagement with a range of stakeholders so its work is strongly evidence-based.[149] Its reports include reviews of Employee Expenses and Benefits, Tax Reliefs, Small Business Taxation, Pensioner Taxation, and Partnership Taxation. It has also reviewed the Competitiveness of UK Tax Administration and developed a Complexity Index for taxation as projects to inform the context of its work.

190. In March 2015 the OTS produced a detailed summary of its work under the 2010–2015 Coalition Government, including a table of recommendations made and implemented.[150] It was however cautious about summarising its work in stark numerical terms, as possibly unrepresentative of progress on its recommendations.

148 HM Treasury, 'Office of Tax Simplification: about us': https://www.gov.uk/government/organisations/office-of-tax-simplification/about [accessed February 2016]
149 Q 60 (John Whiting)
150 Office of Tax Simplification, OTS simplification recommendations: summary at March 2015, March 2015: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/417798/OTS_List_of_Recommendations.pdf [accessed February 2016]

Table 1: OTS Simplification Recommendations, March 2015

	Total	Accepted	Partly accepted	Under review	No response or rejected	Implemented	Partly implemented
Big picture recommendations	60	16	9	22	13	9	7
Other formal recommendations	342	150	24	96	72	109	65

Source: <*https://www.gov.uk/government/publications/ots-list-of-recommendations*>

191. In the Summer Budget 2015 the Chancellor announced the Government's intention to put the OTS on a permanent, statutory footing. The Financial Secretary to the Treasury stated in his letter of 8 July 2015 to Michael Jack, then Chairman of the OTS, and John Whiting, its Tax Director, that: "My vision is for a stronger OTS to play a greater role in the public debate, to provide challenge to HMRC on its important digital agenda, and tackle the big complexities in the system."[151]

The draft legislation

192. Draft Clause 83(1) states simply that: "There continues to be an Office of Tax Simplification" and does not use the term 'independent'.

193. Draft Clause 84(1) defines the general functions of the OTS, primarily, "to provide advice to the Chancellor of the Exchequer… on the simplification of the tax system." Simplification is not defined, but draft Clause 84(3) includes "improving the efficiency of administration" of tax.

194. Draft Clause 85 provides the reporting mechanisms to the Chancellor on reviews of areas of tax law undertaken. The Chancellor must publish and lay these reports before Parliament as well as publish a response.

195. Draft Clause 86 requires the OTS to prepare and publish a report of the performance of its functions in each financial year and the Chancellor must lay such reports before Parliament.

196. Draft Clause 87 requires HM Treasury to review every five years the effectiveness of the OTS in performing its function and publish these reviews.

197. The draft schedule provides the OTS with its constitutional framework, including at paragraph 1 its membership, requiring that all members of the OTS be appointed by the Chancellor. Paragraphs 7 and 11 provide that HM Treasury may provide the OTS with the staff and financial resources as appear to HM Treasury to be necessary for the proper performance of its functions.

198. The functions of the OTS are set out in general terms and could, if the Chancellor so directed, include a broader remit, such as, matters of policy design. Other than in the provision by HM Treasury of finance and resources,

151 Letter, David Gauke MP, Financial Secretary to the Treasury, to Rt Hon Michael Jack and John Whiting, Office of Tax Simplification , 8 July 2015, page 2: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/443524/Summer_Budget_2015_Office_of_Tax_Simplification.pdf [accessed February 2016]

the clauses are silent on the relationship that the OTS should have with HM Treasury and HMRC.

199. The clauses do not place any other obligations on the Chancellor, HM Treasury, HMRC or any other body to give effect to or incorporate the OTS's advice.

OTS activities and achievements

200. Witness evidence recognised that, in its first five years, the role and focus of the OTS had developed. Mr Whiting, the Tax Director of the OTS, commented that its early days were something of an experiment[152] and whilst the early intention was to take a technical and legislative focus, that evolved to embrace the administrative aspects of tax as well.[153]

201. Witnesses agreed that it was not appropriate to measure the success of the OTS only by how many of its recommendations were implemented, as that was not within its control. Implementation depended on the alignment of those recommendations with the priorities of the Chancellor, HM Treasury and HMRC. Cerys MacDonald, of HM Treasury, agreed,

> "the Government, when reflecting on the OTS's recommendations, have to look at tax simplification alongside other objectives which they also seek to achieve through the tax system, whether that is fairness, growth, or the wider fiscal context at each fiscal event, so it is not right to look just numerically at the precise number of recommendations that have been accepted."[154]

202. The decision of the Chancellor to put the OTS on a permanent and statutory footing is in itself a measure of its achievements and approach. It is a credit to the efforts of Mr Whiting, Mr Jack and the OTS staff between 2010 and 2015 that support for its permanent establishment also comes from the spectrum of organisations it worked with in that period.

203. Witnesses from the representative bodies commented positively on the OTS achievements so far, particularly in view of its limited resources. Andrew Chamberlain, of The Association of Independent Professionals and the Self Employed, commented: "We think that the OTS has made a really significant contribution to the simplification agenda" and "the business community finds it very approachable."[155] John Cullinane of the Chartered Institute of Taxation commented, "I think the OTS has done a good job."[156]

204. The success of the OTS might have been more subtle than any numerical analysis might suggest. On behalf of HM Treasury, Ms MacDonald commented:

> "I would not underestimate the influence that the existence of the OTS and our informal relationships and engagement have on the way we approach and think about policy and, importantly, tax administration, where the OTS has shifted mind-sets and put a focus on these areas that they might not have had before."[157]

152 Q 60 (John Whiting)
153 Q 69 (John Whiting)
154 Q 77 (Cerys MacDonald)
155 Q 74 (Andrew Chamberlain)
156 Q 14 (John Cullinane)
157 Q 78 (Cerys MacDonald)

205. In addressing why more of the OTS recommendations had not been implemented, the professional bodies questioned the willingness of the Government to take them forward in practice. On behalf of the Chartered Institute of Taxation, Mr Cullinane suggested: "Tax simplification is not an important enough priority. That is the basic issue."[158] The sentiment was echoed by Chas Roy-Chowdhury from the Association of Certified Chartered Accountants: "I think the OTS really has done as much as it can within the scope and remit it has, but I do not think the Government take simplification seriously enough."[159]

206. It appears from its evidence that HMRC may be more focussed on the implementation of administrative simplification, rather than structural or legislative simplification. This chimes with Mr Whiting's evidence reported earlier.[160] Brian Redford, of HMRC, noted that HMRC had to,

> "look at simplification not just of the tax code but in how we can support customers across the tax-paying base through other means: in other words, simplification of the administrative burden that they have to bear and in the way they do business with us."[161]

207. Emma Churchill, also from HMRC, confirmed that, in relation to the recent '*Making Tax Digital*' initiative, "a lot of the drivers have been about simplification for our customers in the administration of the tax system."[162]

208. Mr Whiting commented that he had hoped for wider support for the principles of tax simplification and the work of the OTS. He reflected that: "one of the possible reasons why we have not achieved more is that members of the House of Commons and the House of Lords have not taken as much interest as we had hoped and have not really got behind a number of our recommendations" and "I would like to see Parliamentary Committees getting hold of that and really questioning why they are not taken through."[163]

209. The way in which OTS recommendations were sometimes implemented by Government came in for some criticism, particularly the cash basis of accounting for small businesses. Originally recommended by the OTS to simplify tax reporting for small businesses with turnover below £30,000, the final legislation applied to larger businesses and incorporated a number of complex restrictions. Professor Judith Freedman commented that the OTS had no control over the implementation of its recommendations: "Cash accounting for example was picked up, taken up, but then implemented in a way that was never intended by the OTS … Once they have made a recommendation, it can just disappear … It may be taken up but not taken up very well."[164]

Resources

210. A number of comments were made about how much the OTS had achieved given the resources allocated to it so far, and how much more it could

158 Q 14 (John Cullinane)
159 Q 14 (Chas Roy-Chowdhury)
160 Q 69, (John Whiting)
161 Q 77 (Brian Redford)
162 Q 77 (Emma Churchill); HMRC, *Making tax easier: The end of the tax return'*, March 2015: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/413975/making-tax-easier.pdf [accessed February 2016]
163 Q 60 (John Whiting)
164 Q 21 (Prof Freedman)

achieve in the future if it had more resources. When asked if putting the OTS on a statutory basis would enhance the possibility of producing more simplification, Robin Williamson from the Low Incomes Tax Reform Group commented: "Yes, if the OTS is considerably strengthened in numbers and resources so that it can get to grips with a larger part of the tax code than it has been able to do so far."[165]

211. The Chartered Institute of Taxation went further and suggested that the draft legislation should clearly ensure that the OTS is given sufficient resources and funding to undertake projects on its own initiative, as well as those it is instructed to undertake by the Chancellor, where, for example, it can demonstrate the need for a review, or it has been encouraged to do so by a sufficient number of interested parties (such as professional bodies).[166]

212. The approaches to resourcing the OTS taken by private sector witnesses and by officials differed. The former looked at the potential for the OTS to do more if it had more resources, whereas HM Treasury, which controls OTS resources, focussed on what the OTS could do most effectively do with the resources provided to it, which did not appear to include getting involved in the policy making process.[167]

213. Witnesses including Professor Freedman questioned how independent the OTS could be in its operations when it is entirely dependent on HM Treasury for funding.[168] Its position was contrasted with that of the Office for Budget Responsibility which is a non-departmental public body.

The role and remit of the OTS

214. There was strong support for the formal establishment of the OTS as an independent body within HM Treasury, but witnesses thought that it was even more important that it was listened to by Government. Its statutory role might be a step forward in gaining greater commitment from Government to achieve greater simplification. Mr Williamson, from the Low Incomes Tax Reform Group, noted that: "If we have this permanent and statutory body, which is consistently funded by the Treasury, that may give it the extra standing necessary to persuade the Government to adopt more of its recommendations"[169] and "the OTS can only realise its full potential if the Government does what it recommends."[170]

215. Other witnesses thought that the role of the OTS had to be considered alongside those of HMRC and HM Treasury in tax simplification, and there should be more focus on other ways in which HMRC and HM Treasury might maximise the benefits that could be achieved from the OTS's efforts. The Law Society of England and Wales strongly supported putting the OTS on a permanent footing but noted that its effectiveness will be dependent in part on "a willingness on the part of HMRC and HM Treasury to respond constructively and promptly to its recommendation."[171]

165 Q 35 (Robin Williamson)
166 Written evidence from the Chartered Institute of Taxation (FBB0003)
167 Q 78 (Cerys MacDonald)
168 Q 20 (Prof Freedman)
169 Q 35 (Robin Williamson)
170 Written evidence from the Low Incomes Tax Reform Group (FBB0011)
171 Written evidence from the Law Society of England and Wales (FBB0008)

216. Evidence submitted by the Association of Independent Professionals and the Self Employed concluded "the Government must be bold and take up the recommendations of the OTS if real simplification is to be achieved."[172]

Consultation and scrutiny of legislation

217. Chris Sanger, from EY, who is also a member of the Forum of Tax Professionals, drew our attention to their report of December 2015[173] and observed that,

> "one of the great successes of the last four years has been the consultation framework, which has helped to ensure that some of the policies being put forward by the Government go through the five-step process and are clear. However, the OTS is completely missing from that framework. There could be a prospective policy role whereby the OTS could feed directly into that framework."[174]

218. The Law Society agreed, suggesting it should be a duty on HMRC to consult the OTS prior to the issue of a consultation to "enable proposals that could undermine the simplification and efficiency goals of the OTS to be reconsidered."[175]

219. The Chartered Institute of Taxation commented that it should also review draft legislation and be "sufficiently resourced to enable it to scrutinise selective proposed legislation, so that it can provide commentary from a complexity perspective."[176]

Development of policy

220. The success of the OTS led a number of witnesses to suggest it should have a role in the development of tax policy. Whilst recognising that the Chancellor needed the flexibility to control fiscal matters and policy direction, it was felt there was a missed opportunity if the OTS did not feature in policy formulation.

221. EY's evidence noted "the absence of the OTS from the active design of new tax policy seems unfortunate. There should be an opportunity for the OTS to utilise the experience obtained from reviewing the current tax system to help Government avoid repeating the same mistakes."[177]

222. A more radical approach to the remit of the OTS was proposed by Professor Freedman: "you cannot simplify tax simply by looking at a few little bits and pieces; you have to look at the whole system and look at it long term. All too often, the OTS is given tasks and required to report within a year, and you cannot simplify like that. They also do not have enough staff, or the right sort of staff, to do any kind of radical work, which is what I am arguing they need to do."[178]

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172 Written evidence from IPSE (FBB0012)

173 Tax Professionals' Forum, *Fourth Independent Annual Report*, December 2015: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/487272/TPF_2015_official_final_16_12_2015.pdf [accessed February 2016]

174 Q 60 (Chris Sanger)

175 Written evidence from the Law Society of England and Wales (FBB0008)

176 Written evidence from the Chartered Institute of Taxation (FBB0003)

177 Written evidence from EY (FBB0018)

178 Q 20 (Prof Freedman)

223. The OTS has not so far been formally involved in policy design and HM Treasury did not regard such a role as appropriate. Ms MacDonald, of HM Treasury, responded to the suggestion by saying: "I would make a distinction between policies that have been developed before they are announced and the role of the OTS in helping us to develop and design the detail of policies once they have been announced."[179] HM Treasury is clearly more cautious about extending the OTS role to internal policy development, suggesting it should be there "leading the public debate on tax simplification."[180] Ms MacDonald also commented: "I would not underestimate the influence the OTS has on how we shape our advice to Ministers on tax policies. We always ask ourselves, "What will the OTS think or say?"[181]

224. Mr Whiting's observation is pertinent here: "to be honest it is a challenge for us to get to the stage where policymakers actually want to involve us."[182]

Reporting on progress in simplifying the tax system

225. Clause 86 requires the OTS to "prepare a report on the performance of its functions" each year. The Chartered Institute of Taxation considered it should also be required to report on the complexity of the tax system and increases or decreases in complexity year-on-year. It saw the lack of this requirement as a question mark over the Government's commitment to reducing complexity.[183]

226. Ms MacDonald, of HM Treasury, noted that the content of the annual report was up to the Chair and Tax Director of the OTS to develop.[184] Clause 84(1) permits the OTS to prepare reports of its own accord, albeit that this would, in practice, be subject to the provision of resources by HM Treasury as noted above.

More complexity is being added

227. Witnesses expressed considerable scepticism about whether real tax simplification might ever be achieved, because successive Governments added complexity to the tax system at a faster rate than the OTS could realistically reduce it. The tax system changed through one or more Finance Bills each year. Even when simplification measures are passed, Bills often include new tax measures which replace or add complexity. This reinforced the view, discussed earlier, that the OTS should have a role in policy design and consultation on draft legislation. Otherwise, as Paul Johnson, from the Institute of Fiscal Studies, put it, the OTS "may be tidying up some mess that was made a few years ago but some more mess is being made without their input."[185]

228. By way of illustration, the first OTS report in November 2010 identified 1,042 tax reliefs in the UK tax system and examined and recommended action on a number of them. 53 are understood to have been removed but new reliefs have been introduced since then, giving 1,156 tax reliefs in statute as at March 2015 (the latest OTS statistics), a net increase of 114.

179 Q 77 (Cerys MacDonald)
180 Q 77 (Cerys MacDonald)
181 Q 78 (Cerys MacDonald)
182 Q 60 (John Whiting)
183 Written evidence from the Chartered Institute of Taxation (FBB0003)
184 Q 77 (Cerys MacDonald)
185 Q 20 (Paul Johnson)

229. Frank Haskew, from the Institute of Chartered Accountants in England and Wales, commented in relation to the period 2010–2015: “the fact is we have had almost 3,000 pages added to the UK tax code, and that was on top of, I think, 9,000 when we started. It is very difficult to simplify a tax system meaningfully when you are faced with that level of extra legislation.”[186]

230. The Federation of Small Businesses commented:

> “Despite the laudable efforts of the OTS … tax continues to pose significant administrative burdens on businesses of all sizes, but particularly the UK economy’s smallest businesses. We see neither the flow of new legislation abating, nor are we convinced that the administrative impact of tax measures undergo the same level of scrutiny as regulation more generally.”[187]

Conclusions

231. **The evidence we have heard is strongly supportive of the work of the OTS and its achievements since it was established, particularly in the light of its very tight resource constraints.**

232. **We welcome the clauses putting the OTS on a permanent statutory footing, but note that witnesses had reservations about the OTS having no role in the development of tax policy, or in avoiding the addition of further complexity. An opportunity is being missed to involve the OTS in policy design. We consider a tax policy design role within HM Treasury for OTS is more important than it being an external scrutineer like the OBR.**

Recommendations

233. **We recommend that the OTS be provided with increased resources to carry out its important role in tax simplification.**

234. **We recommend that the OTS’s statutory remit be extended to give it an integral role in tax policy design.**

235. **We also recommend that the OTS is fully included in consultations on draft tax legislation under the Tax Consultation Framework and that the Framework be amended to accommodate this.**

236. **We recommend that the OTS publish, alongside each Finance Bill, an assessment of the extent to which the measures in the Bill help reduce the complexity of the tax system.**

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186 Q 14 (Frank Haskew)
187 Written evidence from the Federation of Small Businesses (FBB0007)

CHAPTER 6: SIMPLIFICATION AND TAXPAYER COMPLIANCE BURDENS

237. This chapter addresses the overarching themes of this inquiry, simplification and taxpayer compliance burdens, and tries to draw out some general conclusions and areas for action.

238. The chapter considers first how complexity is defined and analysed and how such analysis is applied to the personal taxation measures in the draft Finance Bill 2016. Second we consider five areas for action—applicable to these clauses and to future measures—that would improve the simplicity, administration, and taxpayer compliance burden of this Bill and future tax legislation. We have made specific recommendations about some of these areas in previous chapters; however, these issues also go to the development and implementation of future tax legislation. We stress the importance of consultation, communication, assessing digital readiness, certainty, and scrutiny of implementation.

Complexity of the tax system

239. In presenting the draft Finance Bill 2016 measures examined by this inquiry the Government has claimed that, either in the short or longer term, they each lead to reductions in the complexity of the individual tax or the tax administration system.

Differing forms of 'complexity'

240. Much has been written about the complexity of the UK (and other) tax systems, the different sources of that complexity, how to categorise its different forms and how to measure its impact by means of a 'complexity index'.[188] For the purposes of this inquiry, a useful distinction is the one adopted by the Office of Tax Simplification (OTS)[189] between two broad types of complexity—'technical' and 'administrative'—that can characterise a particular tax provision. 'Technical' complexity is "mainly concerned with policy and legislative flaws and inconsistencies" and how easy a particular statutory provision is to understand.[190] 'Administrative' complexity is concerned with the operational process and the reporting, record-keeping, checking and other tasks that need to be undertaken in order to comply with the provision.

241. Both these types of complexity can affect the various financial, time and psychological costs incurred by taxpayers in meeting their obligations and interacting with the tax system. The two themes of this inquiry, simplification and taxpayer compliance costs, are therefore closely linked. The costs to taxpayers of complying with the tax code are, among other things, a function of the simplicity, stability and clarity of the obligations it imposes. A tax system that is opaque and complicated to understand is more difficult to comply with, and poor compliance can mean greater risks for the Exchequer as well as greater costs for the taxpayer. Broadly speaking, a simpler tax

188 Office of Tax Simplification, *Complexity Index*, June 2015: https://www.gov.uk/government/publications/office-of-tax-simplification-complexity-index [accessed February 2016]

189 Office of Tax Simplification, *Avoiding complexity: the OTS's lessons learned and some principles*, June 2015, p 2, Section 3: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/435704/Principles_of_avoiding_complexity_June_2015.pdf [accessed February 2016]

190 ibid, June 2015, page 2, Section 3

system is easier, and therefore potentially less costly, to administer. As the Federation of Small Businesses put it:

> "A tax system that is simple to understand is also likely to result in greater accuracy and compliance by taxpayers, reduce the need for tax agent advice, and enable businesses to use simpler and less expensive business software. The benefits of reduced error and greater accuracy will flow through to HMRC revenue."[191]

242. The OTS made much the same point: "a more complex tax system is more expensive for taxpayers and they are less likely to get their tax right first time".[192]

Complexity and the savings and dividends proposals

243. The evidence reported in Chapter 2 suggests that the introduction of the Personal Savings Allowance and the abolition of the TDSI reduce 'administrative' complexity insofar as certain taxpayers no longer need to fill in forms claiming exemptions from or repayment of income tax; and, for many people, they remove savings income from the tax net altogether. As the Low Incomes Tax Reform Group and Tax Aid have argued, these changes reduce the compliance burdens of a large number of taxpayers.[193] After the initial costs of making changes to their systems and informing customers have been incurred, they reduce the operating costs of building societies[194] and, presumably, also banks. But they do nothing to simplify the tax system in the 'technical' sense. If anything they add complexity by introducing an allowance whose value depends on the taxpayer's income.

244. By contrast, the abolition of the dividend tax credit does address issues of technical complexity. But as EY and Deloitte[195] suggested, the reform misses the opportunity for further technical (and administrative) simplification by disposing of the complexity of having a different set of marginal tax rates for dividend income (7.5%, 32.5% or 38.1%) than those which apply to other forms of income (20%, 40% or 45%).

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191 Written evidence from the Federation of Small Businesses (FBB0007)
192 Office of Tax Simplification, *Avoiding complexity: the OTS's lessons learned and some principles,* section 1
193 Q 25 (Robin Williamson and Caroline Miskin)
194 Written evidence from the Building Societies Association (FBB0015)
195 Written evidence from EY (FBB0018); Written evidence from Deloitte LLP (FBB0004)

Box 1: Cliff Edges

The income tax system grants many tax reliefs, the majority of which are now only available in full to those on lower incomes. The way in which the reliefs cease to be available can result in unfortunate complexities.

A cliff edge effect occurs where £1 of income over a fixed financial limit removes a tax relief or reduces the amount of the tax relief. For example, the transferrable personal allowance between spouses or civil partners stops once either partner's earnings reach the higher rate limit, to be £43,000 in 2016/17. The Personal Savings Allowance cliff edges will be at £43,000 (when the value of the Personal Savings Allowance reduces from £1,000 to £500) and again at £161,000 (where it reduces to zero).

A taper effect occurs where a tax relief is reduced in value once income exceeds a certain level. That significantly increases the effective marginal rate of tax for a band of income above that level. For example, the personal allowance—to be £11,000 in 2016/17—reduces by £1 for every £2 that income exceeds £100,000. This gives an effective marginal rate of tax of 60% on income between £100,000 and £122,000 when the personal allowance is fully withdrawn and any additional income is taxed at 40%. The same taper effect is seen in the high income child benefit tax charge, to couples with income over £50,000 where effective marginal tax rates are in excess of 50%. Further, in the loss of the annual pensions allowance for those earning over £150,000 where effective marginal tax rates reach 67.5%.

245. Like the introduction of the Personal Savings Allowance, as Chapter 3 makes clear, the new dividend allowance reduces administrative complexity for higher and additional rate taxpayers with dividend income of no more than £5,000. Taken together, the changes to dividend taxation increase compliance complexity for basic rate taxpayers with dividends in excess of the allowance (as does the abolition of the TDSI for some basic rate taxpayers), and for many director/shareholders of small companies.

246. Finally, unlike 'conventional' income tax allowances, neither the savings income covered by the Personal Savings Allowance nor the dividend income covered by the dividend allowance are wholly exempt from tax and they continue to 'count' as taxable income in applying withdrawal tapers for the personal allowance, child benefit entitlement and the marriage allowance. As a result both new allowances introduce new technical and administrative complexities, or 'cliff edges', for those taxpayers on the margins of tax bands. As Professor Judith Freedman of the University of Oxford told us:

> "The worry is that the simplification is in the administration. If you step back and try to understand the system … it looks more and more complicated: it is not very logical and you have all these little different bits of savings allowances and personal allowances and dividend allowances. To actually sit down and understand the system, and how much you are paying and why, is difficult."[196]

247. The main conclusion from this analysis is that a claim that a particular tax measure is a 'simplification' is rarely that simple. A comprehensive assessment of the measure's impact needs to look at both aspects of complexity and to consider the full range of taxpayers affected against the background of all the

196 Q 15 (Prof Freedman)

existing complexities that particular measure interacts with. John Cullinane of the Chartered Institute of Taxation, speaking about the Personal Savings Allowance changes, thought that,

> "because when these ideas, which might sound quite good and appealing, are discussed by a limited number of people, albeit expert, within the context of a massively complicated code already, there are all sorts of interactions with other features and ramifications they do not work out at the time."[197]

248. The impact assessments for the savings and dividend income measures do mention the main taxpayer groups who are likely to see their compliance costs rise. Although there is no attempt to estimate those costs and therefore the basis, other than sheer numbers of taxpayers on either side of the equation, on which the policy trade-off was made. It is surprising, however, in the light of the evidence reported at paragraph 94 above, that the impact assessment for the reform of dividend taxation states that the measure "is expected to have a negligible impact on business or civil society organisations because the impact will mostly apply to individual shareholders."[198]

Reduction of complexity and compliance burdens: areas for action

Appropriate consultation

249. Many of the impacts of a policy change on the complexity of the tax system, and the compliance burdens of those taxpayers affected by it, can be readily identified, and sometimes quantified, by policy analysts at HMRC or HM Treasury. Others cannot, often for lack of relevant experience, insufficient understanding of taxpayer business realities or experience of the tax system. That is why the 'new approach' to tax policy making introduced by the Coalition Government in 2011 requires full consultation with those affected by proposed changes at every stage in the policy-making process. A similar requirement is embedded in the OTS's second principle for avoiding additional complexity: "talk to people who will use or be affected by the legislation; try and see it from their point of view so as to help assess practical issues."[199] Apart from a limited consultation exercise on the abolition of the TDSI, no such consultations took place before the publication of the draft 2016 Finance Bill on either the savings or dividends reforms.

250. **We deeply regret the lack of consultation on the savings and dividend income proposals and repeat the recommendation in our Report on the draft Finance Bill 2014 that the Government should reassert its commitment to the 'new approach' to tax policy making and make sure that, in future, it adheres to it in full except in the most exceptional circumstances.**

Effective communication

251. Another strand of concern to emerge from our inquiry was that, although some measures in the draft Finance Bill 2016—the Personal Savings Allowance, the dividend allowance, the abolition of the TDSI and of dividend

197 Q 4 (John Cullinane)

198 HMRC, *Income Tax: changes to dividend taxation*, December 2015, page 6: https://www.gov.uk/government/publications/income-tax-changes-to-dividend-taxation/income-tax-changes-to-dividend-taxation [accessed February 2016]

199 Office of Tax Simplification, *Avoiding complexity: the OTS's lessons learned and some principles*, section 7

tax credits and the introduction of Simple Assessments—had the potential to simplify the tax affairs of many individuals much depended on their detailed implementation. Many of the risks and costs to taxpayers arise from a lack of awareness of changes to the tax system, and a lack of understanding of what they mean for them individually, of how their responsibilities are affected by those changes and what they need to do in response, in order to comply with tax requirements. As reported in Chapters 2–4, this concern emerged repeatedly in the evidence we heard as did the risks that, through a lack of awareness, taxpayers potentially affected by the changes would simply assume that information provided by HMRC was correct, or that they would fail to review their savings and investments in the light of the changes.

252. Taxpayer compliance costs of this kind can be reduced by well-executed initiatives to inform and educate those affected by the changes, and by well-resourced programs to guide and support those who have difficulty in understanding and complying with changes. HMRC's strategies for communicating the changes to taxpayers and for providing tailored support to those who need it most are vital. The importance of raising taxpayer awareness, good guidance and helplines are emphasised in the OTS's principles for avoiding unnecessary complexity.[200]

253. We were reassured to hear from Emma Churchill of HMRC, in the context of the move to digital tax accounts, that HMRC are aware that special provision will need to be made for the needs of those taxpayers described as 'digitally excluded'[201] and, as our recommendation at paragraph 184 suggests, we look forward to seeing the details of their plans. However, we were alarmed to hear that HMRC's communications 'strategy' for publicising the Personal Savings Allowance and the abolition of the TDSI is so reliant on the banks and building societies and is otherwise essentially reactive and heavily focused on digital channels of communication, in particular GOV.UK. Plans for communicating the dividend taxation changes appear even less fully formed or pro-active.

254. It is also unclear what financial provision, if any, has been made in HMRC's operational plans for communications initiatives. Neither the note accompanying the savings income changes nor that describing the dividend changes makes any mention of them apart from a reference to "increased customer contact" as one of the factors contributing to a total cost of around £1 million estimated to be the operational impact on HMRC of implementing the savings changes.[202]

255. **We do not agree with HMRC that the task of communication can largely be left to institutions, banks, intermediaries and advisers. Nor is it satisfactory simply to direct the individual to HMRC's website. We believe that government has a duty to inform the taxpayer directly, well in advance, of systemic changes that will affect the tax they owe, and how it is collected. The direct link between citizen and tax authority is important, and the authority must, by direct communication, ensure that citizens are aware of their responsibilities.**

200 Office of Tax Simplification, *Avoiding complexity: the OTS's lessons learned and some principles*, section 7
201 Q 86 (Emma Churchill)
202 HMRC, *Income Tax: Personal Savings Allowance*, 9 December 2015: https://www.gov.uk/government/publications/income-tax-personal-savings-allowance/income-tax-personal-savings-allowance#contents [accessed February 2016]

256. **We have made specific recommendations about communications and taxpayer support in respect of the savings income[203] and dividend taxation[204] changes and the introduction of Simple Assessments,[205] but we think the issue is much more general and affects all tax reform proposals.**

257. **We recommend that all major tax reform proposals should be accompanied by a fully funded plan outlining how the changes will be communicated to taxpayers affected by them and how those taxpayers will be guided and otherwise supported so that they can comply with the revised obligations.**

Assessing Digital Readiness

258. We accept, as the OTS does, that some degree of complexity is an inevitable feature of any modern tax system. As we have argued above, the burden of dealing with such systems can be reduced by effective communications and taxpayer support strategies. Recalling his experience at the OTS, John Whiting commented:

> "When we were set up, the vision was that we would tackle the technicalities and metaphorically tear pages out of the tax code. Very quickly it became apparent to me that the administration—and by administration I include everything from how you file your return to the information that is made available—is at least as important. If the underlying law is complex and the interface is simple—a computer analogy—you can manage and achieve it."[206]

259. The burden of complying with the technical and administrative complexities of the tax system can also be reduced by hiding them behind user-friendly computer software. The OTS makes the point thus: "Probably the best route in practice to a simpler tax system is increased digitisation."[207] The introduction of simpler assessments and the Government's '*Making Tax Digital*' agenda are intended to achieve a degree of administrative simplification by this means, and that is why we have welcomed, with some reservations, the proposed direction of travel.

260. One of these reservations is that digital solutions cannot readily be applied across the range of taxpayers regardless of their needs, aptitudes and preferences. As set out at paragraph 173, a significant minority of the tax-paying population were assessed as 'digitally excluded'. Others, who may have access to the necessary technology, may struggle to adapt their working practices to HMRC's digital environment. Caroline Miskin, of TaxAid, commenting on the proposed requirement to keep records in digital form, put it very plainly:

> "At TaxAid, we have never come across a single client who has ever kept electronic tax records … We do not necessarily dispute the direction of travel, but the *Big Issue* sellers, actors, people in the construction industry, gardeners, and the very smallest businesses, where all people are doing is selling their own services, do not keep electronic records

203 Chapter 2, para 63
204 Chapter 3, para 117
205 Chapter 4, para 159
206 Q 69 (John Whiting)
207 Office of Tax Simplification, *Avoiding complexity: the OTS's lessons learned and some principles*, section 8

> and do not find it necessary for their purposes. It will be a huge shift. By 2018 they are going to have to have electronic records. It is going to be an additional something that they will have to do for HMRC purposes, but they will not see any benefit."[208]

261. We have set out in Chapter 4 specific recommendations for measures to be taken to implement the digitisation contained in this draft Bill. The problem described above goes to a wider issue: what is HM Treasury and HMRC's assessment of the digital readiness of taxpayers?

262. **We recommend that the Government when considering further steps in the process to make tax digital, reviews, in consultation with representative groups, the ability and readiness of taxpayers to engage with any new system. For example, the additional obligations on businesses to keep, complete and submit to HMRC quarterly electronic records. At face value this imposes an additional burden that will be felt particularly acutely by small and micro businesses. This would enable the system that is designed, and then implemented, to be the most efficient for both HMRC and the taxpayer.**

Certainty, stability and strategy outlines

263. Another theme that emerged from the evidence we heard was that frequent changes to existing rules can be destabilising, by creating uncertainty and learning costs for taxpayers and making it more difficult for them to take informed long-term decisions and to comply with their tax obligations. In the context of the draft Finance Bill 2016, the concern repeated by many witnesses was that it was not clear whether there was a coherent rationale for introducing two new allowances, with different values and different rules, alongside ISAs and the 0% starting rate for savings income whilst launching a major consultation on the future tax treatment of pension savings (which had already undergone significant changes in most recent Budgets).

264. Paul Johnson, from the Institute for Fiscal Studies, compared the making of tax policy to most other policy,

> "where there are strategies coming out of departments' ears and lots of consultation on good and bad policies. Regarding the high-level direction of tax policy, we get none of that essentially. We have no sense of where we are going on taxation of housing, pensions, or indeed savings, until it is sprung on us. I think some of this is terribly damaging."[209]

265. He went on to say that:

> "The change year after year in taxation of long-term vehicles such as savings and housing is clearly damaging; the new continued increases in stamp duty on the one hand, or reductions in pension tax relief on the other, or changes in buy-to-let. Some of it may be entirely sensible, but it needs to be thought through as a whole, particularly if in one year, for example, you are going to change the rules around annuitisation and tax relief for pensions, and the next year think about the whole structure of pension taxation."[210]

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208 Q 33 (Caroline Miskin)
209 Q 19 (Paul Johnson)
210 Q 19 (Paul Johnson)

266. Other witnesses echoed Mr Johnson's comments. Some claimed, more generally, that many recent Budgets and Finance Bills had introduced piecemeal changes, particularly to the personal tax system, without clear articulation of a coherent overall strategy giving context to individual changes. Moreover, they seemed to have no regard for the complexity added to the system or the consequences for those attempting to navigate it. The absence of strategy and the need for tax changes to fit within a clear roadmap was developed by Chas Roy-Chowdhury from the Association of Chartered Accountants:

> "We find that in every Budget or several Budgets at year—and it is happening now with Autumn Statements—there are a number of changes which seem to happen and which are left-field. You do not expect them, or you do not expect them to land in the way you do when you see the draft legislation. It really goes back to having a roadmap, and if not a roadmap a discussion—let us try and do things properly in tax rather than making the complex tax system ever more complex."[211]

Roadmaps

267. Many witnesses pointed, as an example of best practice, to the corporate tax roadmap published in 2010 which gave businesses a clear idea of the direction in which the Government was planning to take company taxation over a series of Budgets. And they also referred to a 'business tax roadmap' which the Government is planning to publish later this year.

268. However Cerys MacDonald, from HM Treasury, and Brian Redford, from HMRC, expressed little enthusiasm for the idea of a savings and investment roadmap.[212] By contrast it was reassuring to hear Emma Churchill, also from HMRC, say that,

> "On the administrative side, we have sought to give a clear sense of direction, which is why we published the '*Making Tax Digital'* roadmap before Christmas. We are seeking to give both businesses and individuals a clear sense of direction in the way we move forward with the administration of the tax system … It is a balance between wanting to show people a clear sense of direction in an area … and giving room for consultation on the administration on both the business and the individual side."[213]

269. **We suggest that the decision not to publish a roadmap for personal savings and investment is reconsidered, particularly in the wider context of a review of pensions. Taxpayers need to be supported in making longer term plans and taking personal financial responsibility. This point has come up in previous inquiries where we came to the conclusion that we shared the concerns of witnesses in this regard.**[214]

270. **We recommend again, as we did in 2014, that the Government should publish roadmaps for the longer-term development of (at least) those parts of the tax system it proposes to change.**

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211 Q 8 (Chas Roy-Chowdhury)
212 Q 80 (Cerys MacDonald and Brian Redford)
213 Q 79 (Emma Churchill)
214 Economic Affairs Committee, *The Draft Finance Bill 2014* (2nd Report Session 2013–14, HL Paper 146), paras 255–259

271. Continuing on the theme of the lack of strategic direction, some witnesses commented on what they saw as the apparent ambivalence of the Government's position on the complexity of the UK tax system, on the one hand stating its continuing commitment to "a simpler and more transparent tax system"[215] and establishing the OTS, but on the other adding to its complexity at every Budget. It may well be that, as EY suggested, the pursuit of a simpler tax system is futile and we should simply be looking at how to make it less complex for particular groups of taxpayers to engage with—that is to focus on reducing compliance complexity and improving administrative systems.[216] In any case, it would be helpful if the Government were to clarify its position by issuing a clear statement of its long-term strategy.

272. **We recommend that the Government outlines a strategy to address the legislative and administrative complexities in the UK tax system. To this end we recommend that the Government requires the OTS to produce once each Parliament, alongside the five yearly review of the OTS conducted by HM Treasury,[217] an assessment of overall complexity of the current tax system and the scope for simplification.**

Independent scrutiny of HMRC implementation

273. Finally it is worth noting Robin Williamson's (from the Low Incomes Tax Reform Group) comments on the degree of scrutiny HMRC is subject to in its implementation of policy and other changes. He noted that:

> "We are very reliant on HMRC telling us and being transparent about its own data and figures, what it is up to and consulting genuinely, which on the whole it is much more inclined to do now than, say, 10 or 20 years ago, but ultimately it is in a fairly privileged position as far as government departments are concerned."[218]

274. This concern about the apparent absence of external scrutiny of HMRC's implementation of changes, both to make sure they have worked as intended and to learn any 'best practice' lessons that might be relevant elsewhere, was expressed by witnesses giving evidence to our 2011,[219] 2013[220] and 2014[221] inquiries. We have already addressed this for the introduction of Simple Assessments, but our concerns extend much wider to the implementation of all significant tax changes. The OTS takes a similar view in suggesting "a requirement for post-implementation reviews to force a reappraisal of the effectiveness of the rules."[222]

275. **We continue to share the concerns of witnesses regarding the absence of mandatory post-implementation reviews, and we repeat the recommendation in our 2014 Report, that the Government should carry out post-implementation reviews of all significant tax reforms, preferably with the help of independent experts. They should cover**

215 Written evidence from HM Treasury and HMRC (FBB0016)
216 Written evidence from EY (FBB0018)
217 Draft Finance Bill 2016, clause 87
218 Q 37 (Robin Williamson)
219 Economic Affairs Committee, *The Finance Bill 2011* (4th Report, Session 2010–12, HL Paper 158, paras 97–102
220 Economic Affairs Committee, *The Draft Finance Bill 2013* (1st Report Session 2012–13, HL Paper 139), paras 162–169
221 Economic Affairs Committee, *The Draft Finance Bill 2014*, (2nd Report Session 2013–14, HL Paper 146), paras 241–249
222 Office of Tax Simplification, *Avoiding complexity: the OTS's lessons learned and some principles*, section 7

relevant evidence of taxpayer awareness of, and compliance with, the changes in question, such as evidence of the effectiveness of communications initiatives, including taxpayer error rates and call volumes and other enquiry indicators. These reviews should not remain internal to HMRC and HM Treasury but be made publicly available.

SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

Chapter 2: Taxation of Savings

1. The evidence we have heard leads us to conclude that the introduction of the Personal Savings Allowance and the abolition of the TDSI represent useful simplifications for a large number of savers on relatively low incomes. However, we share the concern expressed by witnesses that these changes also bring significant increases in the complexity and compliance burdens faced by over one million higher income savers and particularly those whose incomes take them to the margins of income tax bands. Those affected may include, for example:

    - pensioners whose savings produce sufficient interest to exceed the new allowance. Many will not know of their obligation to report this income to HMRC; and
    - savers on the margins of the tax bands. A saver whose income increases from £43,000 to £43,001 will face an increased tax liability of £100.20 because their tax free allowance will drop from £1,000 to £500. (Paragraph 60)

2. We agree with those witnesses who said that the degree of complexity associated with these changes might have been reduced had consultation taken place in the early stages of policy development. (Paragraph 61)

3. We are very concerned to hear about the low levels of taxpayer awareness of the current system for taxing savings income and that relatively little has so far been done to publicise the changes that come into effect this April and to prepare savers for them. We are not convinced by HMRC's current plans for communicating those changes. (Paragraph 62)

4. We strongly recommend that, as a matter of urgency, HMRC replace their current approach to communications with a comprehensive strategy to make taxpayers aware of the abolition of the TDSI and the introduction of the new Personal Savings Allowance and of recent changes to ISAs and to the starting rate for savings income. This strategy should include a public awareness campaign led by HMRC in partnership with banks, building societies and other financial institutions. Using a wide variety of media, including more traditional approaches, it should aim to inform savers of both their tax obligations and the need to review their savings choices in the light of the changes. (Paragraph 63)

5. We also recommend that the Government review:

    - the drafting of new section 12A Income Tax Act 2007, introduced by draft Clause 1, so as to clarify its meaning; and
    - its decision to retain a requirement to deduct income tax at source from some forms of savings income covered by the Personal Savings Allowance with a view to extending the coverage of the gross payment arrangements to other sources, if possible. (Paragraph 64)

Chapter 3: Taxation of Dividends

6. Although witnesses agreed that taxpayers with relatively small portfolios will eventually find the new dividend allowance and abolition of dividend tax

credits easier to understand than the present system, there were concerns about the added complexity for savers with larger portfolios and for small company directors/shareholds and about the absence of consultation on these proposals. (Paragraph 113)

7. We share those concerns and agree that some of the complexity might have been avoided had there been early consultation in accordance with the Tax Consultation Framework. (Paragraph 114)

8. We are also concerned that HMRC may not have fully appreciated the need for clear and timely communication to taxpayers so that they can continue to make informed personal financial decisions, and meet their obligations, and that companies have not been informed of HMRC's plans for making shareholders aware of the changes. (Paragraph 115)

9. We are not convinced that HMRC's plans to put information on GOV.UK are sufficient to raise the awareness of taxpayers to their new responsibilities without the help of companies paying dividends. (Paragraph 116)

10. We recommend that HMRC urgently develop a comprehensive communications strategy to make taxpayers aware of the changes. In particular taxpayers should be informed:

- what the dividend tax changes mean for them in making appropriate financial decisions, including their impact on ISA savings; and
- how they should use the information they receive from companies to complete their tax returns or check tax assessments they receive from HMRC. (Paragraph 117)

Chapter 4: Simple Assessments and Digital Tax Accounts

Simple Assessments

11. We commend the Government's plans to provide HMRC with the powers to make Simple Assessments of individuals' tax liabilities on the basis of third party information. They have the potential to reduce the compliance burdens imposed on low income taxpayers who are currently required to complete Self Assessment returns. (Paragraph 157)

12. We share the concerns of witnesses about the need to ensure that the data used to make Simple Assessments is accurate and clearly presented in disaggregated form, so that each separate source of income is identifiable, and that those receiving such assessments are aware of their responsibility to check them carefully and dispute them if necessary. We are also concerned about the lack of public information concerning HMRC's plans for rolling out the new assessments and for communicating the changes to taxpayer. (Paragraph 158)

13. We recommend, therefore, that HMRC take action to clarify and publicise: its plans for implementing the new assessments, the responsibilities of taxpayers receiving Simple Assessments and the information they can expect to receive from HMRC and third parties. (Paragraph 159)

14. We are concerned by evidence that the information supplied to HMRC by the Department for Work and Pensions can be the cause of inaccuracies in the current system. Prior to the new arrangements being implemented, and DWP information being used to 'pre-populate' Simple Assessments, we

recommend that HMRC take steps to satisfy itself that this data is robust and accurate. (Paragraph 160)

15. In the light of the evidence submitted in response to the consultation on the draft Finance Bill 2016, we recommend that the Government review the requirement in the draft legislation to dispute a Simple Assessment within 30 days of its being issued. We are concerned that individuals will struggle to obtain, often from third parties, the information necessary to check their assessments and to dispute them within the time limit currently proposed. (Paragraph 161)

16. We also recommend that HMRC produce and publish an analysis of the lessons to be learned from the first full tax year, 2016/17, in which Simple Assessments are implemented in good time to inform subsequent stages in the transition to digital tax accounts. (Paragraph 162)

Digital Tax Accounts

17. We recognise that the Government will be undertaking consultations on the remaining features of the transition to digital tax accounts in the next few months and draft clauses will not be available for scrutiny until December when the draft Finance Bill 2017 is due to be published. (Paragraph 182)

18. We found many of the issues raised in the evidence submitted concerning. Questions remain: how will elderly people who are not confident using online resources manage their tax affairs? How can rural businesses with poor broadband access meet their obligations under a digital system? We conclude that these measures require detailed consideration before policy decisions are taken and draft legislation is made available. (Paragraph 183)

19. We commend the Government for publishing a comprehensive timetable for these consultations and we recommend that they include:

    - a full assessment of the impact of the 'Making Tax Digital' proposals, including any new reporting requirements and compliance costs, on smaller businesses. This should address the significant concerns raised with us by business representatives, particularly the proposed quarterly reporting and the associated possibility of quarterly payments, and include any evidence to support the Government's claims that digital record keeping will yield business benefits;

    - an analysis of any changes in the powers of HMRC and in the obligations of taxpayers as a consequence of the move to digital accounts; and

    - a detailed outline of HMRC's plans to educate and support taxpayers, particularly those not acquainted with, or without access to, new technologies, through the transition to and in the early years of the new system. (Paragraph 184)

Chapter 5: Office of Tax Simplification

20. The evidence we have heard is strongly supportive of the work of the OTS and its achievements since it was established, particularly in the light of its very tight resource constraints. (Paragraph 231)

21. We welcome the clauses putting the OTS on a permanent statutory footing, but note that witnesses had reservations about the OTS having no role in the development of tax policy, or in avoiding the addition of further complexity.

An opportunity is being missed to involve the OTS in policy design. We consider a tax policy design role within HM Treasury for OTS is more important than it being an external scrutineer like the OBR. (Paragraph 232)

22. We recommend that the OTS be provided with increased resources to carry out its important role in tax simplification. (Paragraph 233)

23. We recommend that the OTS's statutory remit be extended to give it an integral role in tax policy design. (Paragraph 234)

24. We also recommend that the OTS is fully included in consultations on draft tax legislation under the Tax Consultation Framework and that the Framework be amended to accommodate this. (Paragraph 235)

Chapter 6: Simplification and Compliance Burdens

Consultation

25. We deeply regret the lack of consultation on the savings and dividend income proposals and repeat the recommendation in our Report on the draft Finance Bill 2014 that the Government should reassert its commitment to the 'new approach' to tax policy making and make sure that, in future, it adheres to it in full except in the most exceptional circumstances. (Paragraph 250)

Communication

26. We do not agree with HMRC that the task of communication can largely be left to institutions, banks, intermediaries and advisers. Nor is it satisfactory simply to direct the individual to HMRC's website. We believe that government has a duty to inform the taxpayer directly, well in advance, of systemic changes that will affect the tax they owe, and how it is collected. The direct link between citizen and tax authority is important, and the authority must, by direct communication, ensure that citizens are aware of their responsibilities. (Paragraph 255)

27. We have made specific recommendations about communications and taxpayer support in respect of the savings income and dividend taxation changes and the introduction of Simple Assessments, but we think the issue is much more general and affects all tax reform proposals. (Paragraph 256)

28. We recommend that all major tax reform proposals should be accompanied by a fully funded plan outlining how the changes will be communicated to taxpayers affected by them and how those taxpayers will be guided and otherwise supported so that they can comply with the revised obligations. (Paragraph 257)

Digital Readiness

29. We recommend that the Government when considering further steps in the process to make tax digital, reviews, in consultation with representative groups, the ability and readiness of taxpayers to engage with any new system. For example, the additional obligations on businesses to keep, complete and submit to HMRC quarterly electronic records. At face value this imposes an additional burden that will be felt particularly acutely by small and micro businesses. This would enable the system that is designed, and then implemented, to be the most efficient for both HMRC and the taxpayer. (Paragraph 262)

Strategy and Roadmaps

30. We suggest that the decision not to publish a roadmap for personal savings and investment is reconsidered, particularly in the wider context of a review of pensions. Taxpayers need to be supported in making longer term plans and taking personal financial responsibility. This point has come up in previous inquiries where we came to the conclusion that we shared the concerns of witnesses in this regard. (Paragraph 269)

31. We recommend again, as we did in 2014, that the Government should publish roadmaps for the longer-term development of (at least) those parts of the tax system it proposes to change. (Paragraph 270)

32. We recommend that the Government outlines a strategy to address the legislative and administrative complexities in the UK tax system. To this end we recommend that the Government requires the OTS to produce once each Parliament, alongside the five yearly review of the OTS conducted by HM Treasury, an assessment of overall complexity of the current tax system and the scope for simplification. (Paragraph 272)

Post Implementation Scrutiny

33. We continue to share the concerns of witnesses regarding the absence of mandatory post-implementation reviews, and we repeat the recommendation in our 2014 Report, that the Government should carry out post-implementation reviews of all significant tax reforms, preferably with the help of independent experts. They should cover relevant evidence of taxpayer awareness of, and compliance with, the changes in question, such as evidence of the effectiveness of communications initiatives, including taxpayer error rates and call volumes and other enquiry indicators. These reviews should not remain internal to HMRC and HM Treasury but be made publicly available. (Paragraph 275)

APPENDIX 1: LIST OF MEMBERS AND DECLARATIONS OF INTEREST

The Members of the Economic Affairs Committee which conducted this inquiry were:

Lord Bilimoria
Baroness Drake
Lord Forsyth of Drumlean
Lord Hollick (Chairman)
Lord Kerr of Kinlochard
Lord Monks*
Baroness Noakes
Lord Teverson
Lord Turnbull
Baroness Wheatcroft
*Lord Monks was unable to attend most meetings.
Mr Tony Orhnial and Ms Elspeth Orcharton were appointed as Specialist Advisers to the inquiry.

Declarations of Interest

Lord Bilimoria

Chairman, Cobra Beer Partnership Ltd

Non-executive Director and Senior Independent Director, Booker Group plc (food wholesaler)

Minmar (900) Limited (business services)

BHL Group (home and leisure products)

Bilimoria & Bilimoria LLP

General Bilimoria Wines Limited

Cobra India Beer Limited

Cobra India New Company Limited

Chairman, Molson Coors Cobra India Private Limited

Chairman, Faridoon Wines Ltd

Consultancy fees for the Member's professional services are paid by Molson Coors Brewing Company (UK) to Bilimoria Holdings Limited (see category 4(a))

Fees for the Member's speaking engagements are paid by The London Speaker Bureau to Bilimoria Holdings Limited (see category 4(a))

Bilimoria Holdings Limited (holding company)

Cobra India Newco

Booker Group plc (food wholesaler)

Residential properties in London and Cape Town

Visit to Ahmedabad, India, 5–12 January 2015, as part of Ministerial delegation and to attend Pravasi Bharatiya Divas (non-resident Indian Day); flights and accommodation paid by Government of India and Federation of Indian Chambers of Commerce and Industry

Guest at the dinner held in connection with the All Party Parliamentary Beer Group Annual Beer Awards, 7 July 2015

Director and Member, Ditchley Foundation

Advisory Board, Seven Hills (public relations/communications firm)

Member, Advisory Board, Judge Business School, Cambridge University

Member, Advisory Board, Birmingham Business School

Member, Vice Chancellor's Circle of Advisors for India, Cambridge University

Visiting Professor, London Metropolitan University

Member, Advisory Board, Cranfield School of Management

Board of Directors, Harvard Graduate School Leadership Institute

President, UK Council for International Student Affairs (UKCISA)

Chancellor, University of Birmingham

National Champion, National Council for Graduate Entrepreneurship (NCGE)

Visiting Entrepreneur, Centre for Entrepreneurial Learning, University of Cambridge

Member, London Business School Foundation for Entrepreneurial Management, Enterprise 100

Chairman, Advisory Board, Cambridge University

Advisory Board Member, Roundhouse Trust

Ambassador, British Library Business and IP Centre

Member, E20 Steering Group (advocacy group for entrepreneurs to engage with, inspire and support enterprise in UK)

Founding Chairman, UK-India Business Council

Founding Member, Indian Prime Minister's Global Advisory Council of Overseas Indians

Trustee, Cobra Foundation

Trustee, British Cardiac Research Trust

Member, Advisory Council, CIDA Foundation UK

Member, Advisory Board, Adab Trust

Co-Chairman, Advisory Board, Loomba Foundation (education of poor widows and children all around the World)

Enterprise Leader, Prince's Trust

Member, UK-India Round Table

Member World Presidents' Organization (WPO)

Member, Chief Executives' Organization

Companion, Chartered Management Institute

Member, Memorial Gates Committee

Champion, Roko Cancer Appeal (MKC Trust)

International Envoy, London

Co-founder, Pictoso (photo-sharing app)

Baroness Drake

On the Board of the Pensions Advisory Service

Advisor to the Tax Incentivised Savings Association

Trustee of Telefornica Pension Scheme

Trustee of Santander Group Pension Scheme

Independent Member of the Private Equity Reporting Group

Lord Forsyth of Drumlean

Non-Executive Director-Secure Trust Bank plc

Owner of property in Scotland used for holiday rentals

Lord Hollick (Chairman)

Member, Advisory Board, Jeffries Inc (Financial Services-work confined to advising corporates on corporate development)

Lord Kerr of Kinlochard

Deputy Chairman of an Energy Company

Director of an Investment Company

Trustee of a charity

In receipt of a public service pension

Lord Monks

No relevant Interests

Baroness Noakes

Director, Royal Bank of Scotland Group plc. Baroness Noakes did not participate in the parts of the inquiry relating to the taxation of savings.

Interests in a wide variety of listed shares as disclosed in the Register of Interests, including:

HSBC Holdings plc (banking)

Standard Chartered Bank plc (banking)

Royal Bank of Scotland Group plc (banking)

Legal & General plc (insurance)

St James's Place plc (financial services)

Standard Life plc (investment management)

Lord Teverson

Fellow of Chartered Institute of Security and Investment

Lord Turnbull

Holds a range of financial savings products, mostly in collective investments.

Holdings of shares of less than £250,000

No trading business interests

Baroness Wheatcroft

Non-executive Director, St James's Place plc (financial services). St James Place provides investment advice to high net worth individuals. Baroness Wheatcroft did not participate in in the parts of the inquiry relating to the taxation of dividends or savings income.

A full list of Members' interests can be found in the Register of Lords Interests: http://www.publications.parliament.uk/pa/ld/ldreg.htm

Tony Orhnial, Specialist Adviser

Trustee, Child Poverty Action Group

Elspeth Orcharton, Specialist Adviser

Member of ICAS Scottish Taxes Sub-Committee

APPENDIX 2: LIST OF WITNESSES

Evidence is published online at www.parliament.uk/finance-bill-2016-sub-committee and available for inspection at the Parliamentary Archives (020 7219 5314).

Evidence received by the Committee is listed below in chronological order of oral evidence session and in alphabetical order. Those witnesses marked with * gave both oral evidence and written evidence. Those marked with ** gave oral evidence and did not submit any written evidence. All other witnesses submitted written evidence only.

Oral evidence in chronological order

**	Mr Frank Haskew, Head of Tax Faculty, Institute of Chartered Accountants in England and Wales	QQ 1–24
*	Mr John Cullinane, Director of Tax, Chartered Institute of Taxation (CIOT)	
**	Mr Chas Roy-Chowdhury, Head of Taxation, Association of Chartered Certified Accountants	
**	Mr Paul Johnson, Director, Institute for Fiscal Studies	
**	Professor Judith Freedman, Oxford University Said Business School	
*	Mr Robin Williamson, Technical Director, Low Incomes Tax Reform Group (LITRG)	QQ 25–37
**	Ms Caroline Miskin, Technical Director, Tax Aid	
**	Sue Martin, VAT and Operational Tax Director, Lloyds Banking Group	QQ 38–59
**	Grace Stevens, Group Director Tax, L&G Group	
**	Keith Richards, Chief Executive, Personal Finance Society	
**	Dermot Callinan, Head of UK Private Client, KPMG	
**	John Whiting, Chief Executive, Office of Tax Simplification	QQ 60–76
**	Chris Sanger, Global Head of Tax Policy, Ernst & Young	
*	Mike Cherry, Policy Director, Federation of Small Businesses (FSB)	
*	Andrew Chamberlain, Deputy Director of Policy, The Association of Independent Professionals and the Self Employed (IPSE)	
*	Mr Brian Redford, Director of Specialist Personal Tax, Her Majesty's Revenue & Customs (HMRC)	QQ 77–90
*	Ms Emma Churchill, Director of Process Transformation, Her Majesty's Revenue & Customs (HMRC)	
*	Ms Cerys MacDonald, Deputy Director, Personal Tax, Her Majesty's Treasury (HMT)	

Alphabetical list of all witnesses

	Association of Taxation Technicians	FBB0002 FBB0009
	British Bankers' Association (BBA)	FBB0005
	Building Societies Association (BSA)	FBB0015
*	Chartered Institute of Taxation (CIOT)	FBB0003
	Crunch Accounting	FBB0001
	Deloitte LLP	FBB0004
*	Ernst & Young LLP	FBB0018
*	Federation of Small Businesses (FSB)	FBB0007
	Freelancer and Contractor Services Association (FCSA)	FBB0010
*	Her Majesty's Revenue & Customs	FBB0016
		FBB0017
*	Her Majesty's Treasury	FBB0016
		FBB0017
*	Low Incomes Tax Reform Group (LITRG)	FBB0011
		FBB0014
	PRISM	FBB0018
*	The Association of Independent Professionals and the Self Employed (IPSE)	FBB0012
	The Law Society of England and Wales	FBB0008

APPENDIX 3: CALL FOR EVIDENCE

The House of Lords Economic Affairs Committee has set up a Finance Bill Sub-Committee (the FBSC) to inquire into the draft Finance Bill 2016 which was published on 9 December 2015.

The FBSC's inquiries focus on technical issues of tax administration, clarification and simplification rather than on rates or incidence of tax.

This year the FBSC will concentrate its inquiry on the extent to which the measures proposed in the draft Bill contribute to the simplification of the personal tax system and their impact on the compliance burdens of individual taxpayers. The FBSC invites evidence on these cross-cutting issues with particular reference to the following three topics:

1. Proposed changes to the taxation of savings and dividends

   The first topic covers clauses (1)–(4) of the draft Bill and the accompanying schedules. The draft clauses reform:

   - the taxation of savings by introducing a new Personal Savings Allowance of up to £1,000 and abolishing the Tax Deduction Scheme for Interest (TDSI) (under which banks, building societies and other institutions deduct tax from interest they pay on deposits held by individuals, partnerships and trusts); and
   - the taxation of dividends by abolishing dividend tax credits, introducing a new tax-free dividend allowance covering the first £5,000 of dividend income, and applying special rates of tax to any dividend income exceeding the allowance.

2. Simple Assessments

   The second topic relates to Clause 71 of the draft Finance Bill which introduces a new power allowing HMRC to assess an individual's tax liability, without a tax return being submitted, using information it already holds (whether received from the individual or a third party).

   This provision is part of the Government's strategy, entitled 'Making Tax Digital', which will lead to the introduction of digital tax accounts (planned for 2017) and the eventual abolition of the tax return. The FBSC is particularly interested in the proposed administration of simple assessments.

3. Office of Tax Simplification

   The third topic covers Clauses 83–88 which establish a permanent Office of Tax Simplification (OTS) and define its functions in statute. The FBSC would welcome views on the extent to which an OTS as constituted by these clauses is likely to promote the future development of a simplified tax system.

Timetable

The written submissions will guide the FBSC's deliberations in oral evidence sessions and also inform their final conclusions and recommendations.

Written evidence should be sent to the Sub-Committee by **29 January 2016**. Public hearings will be held in January and February 2016. The report will be published before the Budget in March 2016.