Making Taxes Simpler

The final report of a Working Party chaired by Lord Howe of Aberavon

July 2008

Executive Summary

The UK tax system has become hugely more complex during the last decade and now cries out for simplification. Within the last year we have overtaken India as the country with the longest tax code in the world. Complexity not only adds to compliance costs and uncertainty, but it also undermines public trust in the tax system itself. The result is that public anger at a series of 'stealth taxes' has reached new heights.

Over the same period the capacity of Parliament to scrutinise tax legislation has been overwhelmed. Several unfortunate episodes over the last year – including the changes to capital gains tax, the taxation of non-domiciles and the 10p tax rate debacle – have dramatically underlined the need to reform the way we make tax law in this country. Individually each of these episodes has been damaging, but collectively they have served to undermine the reputation of the UK as a stable environment in which to work, save and invest.

This is the final report of a Working Party led by Lord Howe of Aberavon and established last year by the Shadow Chancellor, George Osborne MP, to take forward the recommendations of the Forsyth Tax Reform Commission regarding the making of tax law.

The main conclusions are:

- The next Conservative Government should establish an Office of Tax Simplification (OTS) to examine the existing tax code and make proposals for simplification. The OTS would operate in a similar way to the National Audit Office, reporting to a new Joint Parliamentary Select Committee on Taxation and overseen by a Steering Committee appointed by the Chancellor of the Exchequer. As well as staff from HMRC and academia, the OTS should also include individuals from the tax professions to provide expertise and a fresh perspective. The OTS would become an authoritative and independent voice on tax law, creating a powerful institutional pressure for simplification of the tax system.

- In order to strengthen parliamentary oversight of tax legislation, the next Conservative government should establish a new Joint Parliamentary Select Committee on Taxation (JPSCT), with membership drawn from both Houses. The new committee would significantly improve the scrutiny of Government initiatives and proposals, and would receive written and oral evidence from external experts. It would also examine and make recommendations on proposals presented to it by the OTS. The new committee would have no power to initiate tax changes nor to erode or compromise the exclusive privilege of the Commons when it comes to the rates and incidence of taxation.

- Finally, and certainly not least important, the next Conservative Government should introduce and entrench a strong, new convention that any changes to tax law with technical content should be proposed no later than the Pre-Budget Report before the Finance Bill in which they are to be included. Such a convention would have avoided many of the problems we have seen over the last year, with badly thought through proposals produced with little consultation and last minute legislation rushed through Parliament without sufficient scrutiny.

Together, we believe that these reforms would revolutionise the framework within which we make tax law, and over time would help to deliver the simpler and more transparent tax system that we so desperately need.

Members of the Working Party

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Kwasi Kwarteng, former Chairman of the Bow Group and Conservative Parliamentary Candidate in Brent East in 2005

Andrew Tyrie MP

1. Introduction

1.1 During the last decade, the tax system has, partly deliberately, been made much more complicated and it urgently needs to be simplified. Over the same period the capacity of Parliament to scrutinise tax legislation has been overwhelmed.

1.2 Our Working Party was accordingly established last year by the Shadow Chancellor, George Osborne MP, to advise upon the action necessary to carry forward the recommendations of the Forsyth Tax Commission Report, *Tax Matters – Reforming the Tax System* **(**published in October 2006 and hereafter referred to simply as "Forsyth"). We have also had the benefit of studying the texts[1] of the Hardman lectures, given by two of our members, Adam Broke and Lord Howe respectively, both of whom made recommendations in this field, together with two reports commissioned by the Tax Law Review Committee of the IFS, namely *Parliamentary Procedures for the Enactment of Rewritten Tax Law*, November 1996 and *Making Tax Law*, March 2003

1.3 Fortified by that analysis, our aim has been to amend, expand or elaborate the proposals in Chapter 9 of Forsyth, which describe the institutional changes believed to be necessary. The Report takes as its starting point (and rightly so) the proposition that the UK direct tax system cries out for simplification and reduction in scale. To this end, it proposes that the processes of pre-legislative consultation and Parliamentary scrutiny should be strengthened and intensified – in particular by the establishment of a Joint Parliamentary Select Committee on Taxation ("JPSCT") and that a new body (the Office of Tax Simplification "OTS") should be given the specific task of simplifying the legislation and reducing its volume.

1.4 Pre-legislative consultation is still too often regarded by Governments as a luxury. Where a major systemic change is being proposed, there can sometimes be time for measured discussion in advance about the principles and the draft legislation. But where it is a change which is seen only by Government as desirable – the abolition of a reduced rate band, for example – or where it is intended to secure a particular change in taxpayers' behaviour, it is less likely to receive meaningful consultation, in the sense of a willingness to listen to adverse views being expressed by the consultees. And in the case of anti-avoidance legislation there is rarely any significant consultation before the event, for fear of forestalling action being taken.

1.5 In similar fashion, the present constitutional arrangements do not permit adequate time for proper line-by-line scrutiny of legislation contained in Finance Bills. There are several reasons for this. Firstly, the volume of legislation in each Finance Bill has increased very substantially over recent years, while the time available for scrutiny has remained the same. Secondly, the Provisional Collection of Taxes Act imposes (not without reason) a timetable, whereby enactment must be achieved by 5 August in each year. Thirdly, scrutiny has had to be undertaken solely by members of the House of Commons - while it has remained (as emphasized by the Chartered Institute of Taxation "CIOT") "impossible to draw upon the wealth of expertise that is available in the Lords". And fourthly, time pressures mean that there is very tight time-tabling of the Standing Committee's scrutiny, amounting to the routine imposition of a guillotine, which severely restricts the opportunity for constructive, detailed consideration.

1.6 Moreover, there is no institutional pressure for change outside the professional bodies and think tanks, which are themselves broadly united in proposals for reform and in criticism of the present position. The CBI sums up an important part of the case[2] by calling, for example, for "formalisation of a 'no surprise' consultation process (including on policy), clear objectives and wide representation".

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1 See British Tax Review (2000) p.18 and (2001) p.113

2 Report by CBI Tax Task Force, March 2008

2. Legislative procedure

2.1 Proposal 37 of Forsyth reads as follows "All changes to the tax law with any technical content to be included in the annual Finance Act must be proposed no later than the preceding Pre-Budget Report ("PBR") (unless in exceptional cases the Treasury can make a convincing case for urgency)". It might seem unrealistic to suppose that Governments would impose upon themselves a self-denying ordinance, which would involve this kind of undertaking in every case, but a competent and determined administration should be able to establish a strong convention to that effect.

2.2 If adopted, this would ensure that new legislation was exposed to a period of detailed public scrutiny, well before the (hitherto conventional) Parliamentary processes commenced. During that time the professional and industry bodies concerned with taxation matters would have the opportunity to raise issues and make representations. It would also enable the JPSCT (see paragraph 1.3 and Section 3) to hold hearings at which evidence could be given by experts and others and the proposals examined in some detail. Forsyth is rightly quite clear that the additional time allowed in this way will improve the quality of the legislative result.

2.3 It is also important that the pre-legislative consultation procedure is appropriate. The introduction of the so called "non-doms" provisions (the structural changes, rather than the £30,000 charge) provides an object lesson in how not to legislate. True, draft clauses were produced for consultation but these were riddled with errors and conceptually unsound in many places. Amendments were made, often with the help of outside professionals, but the legislation was far from constituting a coherent code when the Finance Bill was published. Substantial and essential amendments were still being produced at a late stage, leaving insufficient time for adequate scrutiny both in and outside Parliament.

2.4 The question of forestalling has in the past been a difficult one. In relation to anti-avoidance legislation it is clearly important that taxpayers are not given an opportunity to take advantage of loopholes, which have been publicised - and that has generally been the reason given for the lack of forewarning and prior consultation. However, this concern has led to some spectacular "own goals", where attempts to close opportunities for tax avoidance have had the opposite effect, largely because not enough time, thought and consultation was invested in designing a replacement that was structurally sound. Examples of recent failures are the 2003 (and subsequent) legislation on Share Schemes (where a significant structural change was made, which resulted in several new avoidance schemes) and the successive changes (2002, 2003 and 2004) in relation to Discounted Securities (where minor amendments intended to block avoidance schemes misfired). The introduction of requirements governing disclosure of tax avoidance schemes has meant that HMRC can react much more quickly to such schemes and the danger of significant tax leakage is much lower than in the past. Exposure and consultation on new proposals should be the presumption in all cases, with departures from the practice being very rare.

3. Office of Tax Simplification (OTS)

3.1 Probably the most substantial innovation proposed by Forsyth (Proposal 39) is the establishment of the Office of Tax Simplification ("OTS") – which may be seen as a rather more descriptive name for the Tax Law Commission, proposed and supported by the CBI and CIOT. This lies at the heart of the proposals and is a key element in any attempt to start a process of simplification and legislative reduction. The not dissimilar Tax Law Rewrite Project ("TLRP") (whose work is now moving towards a conclusion) has been a constructive and valuable agent for change in the manner, style and language of fiscal legislative drafting, Its influence may now be seen in other legislative fields. However, its terms of reference are strictly circumscribed[3], in that the rewriting process may not alter the sense of the law in any but the most minor detail.

3.2 The OTS would have a much wider remit to examine such areas of fiscal law as seemed to it appropriate and to put forward proposals for tax law reform and simplification. Plainly it could not have any authority over questions affecting tax rates or yield. An appropriate mechanism for identifying the likely budgetary effect of its proposals would in any case be essential.

3.3 Forsyth envisages that the OTS would operate in much the same way as the National Audit Office and would become "an authoritative, independent voice on tax law". In order to achieve this, OTS would need Parliamentary backing. It is expected that this should be forthcoming from the JPSCT, to which OTS would report and which would have power to conduct hearings. OTS would also need to have ready access to, and be able to obtain the cooperation of, government departments – most important, of course, the Treasury and HMRC. Success for OTS along these lines should establish and institutionalise , in the words of our Chairman (in his 2001 Hardman lecture), "a process, whose continuing insistence on simplicity is as irremovable, and as constantly present, as the voice of the tax-raising departments – and as the politically restless, impatient input of successive Chancellors".

3.4 Forsyth proposes that, in addition to its role in reviewing existing tax law, OTS would examine proposed new legislation, to determine whether it was consistent with the principles of sound tax law and was reasonably simple. It is doubtful, in the early years at least, just how far this would be practicable within OTS's likely resources. This suggests that part, at least, of this undoubtedly desirable function should also be undertaken by the JPSCT - assisted by the representative bodies, as discussed above. One reason for saying this is that it could be disruptive to any deliberative organisation (such as OTS), if once a year part of its team had to divert its attention to examination of PBR proposals. Even so, we should expect there to be increasing dialogue between OTS and those officials within the Treasury and HMRC, with responsibility for the development of fresh proposals - in much the same way as consultation currently takes place with the Tax Law Rewrite team

3 Despite this it has identified over 200 areas where simplification seemed to it desirable and which have been passed to HMRC for review. – a process which could now be undertaken by the OTS

3.5 We suggest that the OTS should be staffed in a similar way to the Law Commission. Its core staffing would be drawn from academics and HMRC and it would probably be led by a senior HMRC official. It should also include some individuals drawn from the professions - whether on secondment or on two to three year contracts. It should, of course, have access to drafting expertise. Estimates of the cost of the TLRP suggest a figure of £3m per annum and we envisage that the OTS might cost much the same.

3.6 The work of the OTS would be overseen by a Steering Committee appointed by the Chancellor of the Exchequer, in a way rather similar to the Tax Law Rewrite Project, and would have much the same kind of membership. It could include members of both Houses, representatives from each of the tax professions (accountancy and law, including some academics and at least one with tax-specialist judicial experience) as well as "consumer-representative" taxpayers and a senior HMRC staff member. The Steering Committee would, amongst other things, be involved in the OTS choice of tasks and oversee the publication of its reports.

4. Joint Parliamentary Select Committee on Taxation ("JPSCT")

4.1 Forsyth's Proposal 38 recommends the creation of a body, which could and should provide more effective Parliamentary oversight of fiscal legislation, namely a Joint Select Committee on Taxation ("JPSCT") with membership drawn from both Houses (The recently appointed Joint Committee(s) on Human Rights and Constitutional Reform, for example, offer encouraging precedents for such cooperation between the two Houses). The proposal of such partnership in this fiscal context is widely supported by tax professionals, being seen as a constructive response to two complementary factors: on the one hand, the widely acknowledged inadequacy of Commons' scrutiny of Finance Bills – in the words of one experienced MP, "no more than a pointless ritual"; and on the other hand, the availability in the Lords of an extensive (but under-employed) diversity of financial expertise.

4.2 Forsyth makes it clear that the JPSCT would have no power to initiate tax changes, but would mainly be scrutinising Government initiatives and proposals. It would also examine and make recommendations on proposals presented to it by the OTS. The JPSCT would, therefore, and as a matter of course, (having received written and oral evidence from the representative bodies) be holding sessions – probably peaking in March or April of each year – to complete their appraisal of the Government's PBR proposals. It would be just at this stage, of course, that the annual Finance Bill would normally be introduced.

4.3 So, one of the two most important questions still to be answered is just how far, if at all, the JPSCT could or should be involved in consideration or treatment of that Bill (implementing, as inevitably it would be, some or all of the PBR tax proposals, which the JPSCT had itself been considering during the preceding six months). Commonsense would surely dictate only one *affirmative* answer to that question.

4.4 The second question has rightly been identified as equally important, by the Commons Members of our Working Party**:** would this involvement of members (or a Committee) of the House of Lords (even if in partnership with the Commons) amount to any kind of encroachment upon the financial privileges of the House of Commons? Virtually the same question has already been addressed, in the context of the Lords' establishment of a Finance Bill Sub-Committee of their Economic Affairs Committee ("FBSC"). This was accompanied by a Lords' decision, on 24 July 2002, "to prohibit the sub-committee from investigating the incidence or rates of tax and to allow it only to address technical issues of tax administration, clarification or simplification". The effect of this limitation was later considered, at the request of the Government, by the Joint Committee on "Conventions of the UK Parliament"[4], which reached the following conclusion:

"The Lords committee should continue to respect the boundary between tax administration and tax policy, to refrain from investigating the incidence or rates of tax, and to address only technical issues of tax administration, clarification and simplification. Provided it does so, we believe there is no infringement of Commons financial privilege."

The FBSC now has a track record of having scrutinised important aspects of the last five Finance Bills 2003-07, and published their Reports and recommendations in time for consideration in Report stage in the Commons. Both in and out of Parliament, the reaction to this work has been distinctly positive.

4 HC 1212 (3 November 2006), Para 244. This Joint Committee Report was subsequently debated and approved by both Lords and Commons (respectively 16th and 17th February 2007).

4.5 An even closer precedent for the prospective work-load of the JPSCT is to be found in the record of the Joint Committee of both Houses, which has handled (over the last ten years) the four substantial Rewrite Bills so far produced by the Tax Law Rewrite Project. The procedure for this stream of legislation was recommended by the first of the IFS Task Forces mentioned in paragraph 1.1 above. Each Bill has been given a Second Reading in the Commons and then passed to a Joint Committee of both Houses, with a majority of Commons members, and an MP in the Chair. That Joint Committee is always under strict instructions to confirm that the Bill is confined to a re-write and simplification of the law, without any significant change. And from the Joint Committee the Bill can go back to the Commons, either to a Committee of the whole house or Report stage (or both) and then to Third Reading[5]. This ensures that the Commons have effectively the last word on the shape and content of the Bill, after it has been dealt with by the Joint Committee. For when the Bill moves on from the Commons to the Lords, it is treated in practice in the same way as every Finance Bill since 1911 – debated at Second Reading only and no amendments tabled, with the Lords throughout acknowledging the primacy of the Commons in the fiscal field.

4.6 These precedents show the Commons, in course of their consideration of several Finance Bills, accepting significant input from the Lords - in the first case, direct from a Lords Sub-Committee and in the second, through the working of a Joint Committee of both Houses. In each case it has been made clear that the partnership must not be allowed to compromise the exclusive privilege of the Commons on the rates and incidence of taxation. This enables us to conclude that similar procedures ought now to be designed and put into practice, to secure the effective functioning of the JPSCT, without any threat to the Commons privileges in the fiscal field. It will be important to meet the reservations of members of the House of Commons on this front.

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5 In practice, every TLRP Bill so far has proceeded straight from Joint Committee to Third Reading – and then through the Lords.

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