



HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ

**Angela Knight CBE, Chair  
& John Whiting OBE, Tax Director  
Office of Tax Simplification  
1 Horse Guards Road  
London SW1A 2HQ**

16 March 2016

*Dear Angela & John*

## **UPDATE ON TAX SIMPLIFICATION MEASURES**

The Chancellor made several announcements relating to the work of the Office of Tax Simplification (OTS) at Budget. I am writing to explain these in more detail, highlight wider areas of interest and set out the topics of your next reviews. I would also like to thank you and your team for your excellent work since the Autumn Statement.

### **Business tax roadmap**

You will have seen that we published a roadmap setting out our plans for business taxes to provide businesses with certainty. It includes much of interest to the OTS, of which I want to highlight four issues.

First, the roadmap commits to significant investment in HMRC to improve its customer service. By 2017, HMRC will provide a 7-day a week service, with extended hours and Sunday opening for online services and tax and tax credit phone lines. HMRC will introduce a dedicated phone service for new businesses and will recruit over 800 new staff into its call centres to improve call waiting times.



Second, the Government will modernise the corporation tax rules for losses, resulting in a more flexible system for business. This builds upon a major recommendation from your competitiveness review and relates to your future work on corporation tax.

Third, the roadmap states our intention to consider reforms to make the tax system fairer and more sustainable, with a more level playing field for people working for themselves regardless of their business structure. You considered this issue as part of your small companies review and it also relates to your future work.

Finally, building on your past recommendations, the Government will abolish Class 2 NICs in April 2018. In future, the self-employed will be able to build contributory benefit entitlement through a reformed Class 4 NICs. This will be a long overdue modernisation of the complex and outdated self-employed National Insurance system.

### **Small companies review**

Thank you for your review of the taxation of small companies. The Government will accept or further consider nearly all of your recommendations, as detailed in the annex to this letter.

I particularly welcome your proposal to develop the design of a look-through taxation system and a new, simple business model that would provide the self-employed with limited liability for their assets. I encourage you to work with the Government and the business





community to further consider how these policies might work in practice and any implementation issues that could arise.

The one recommendation that I have not accepted is for a study of a consolidated turnover tax. As your report notes, a tax based on turnover would fail to take account of a business's expenses and, consequently, its profitability, leading to distortions and unfair outcomes between different types of businesses.

I believe that Making Tax Digital can achieve many of the simplification benefits of a turnover tax without the distortions by making it feel like businesses are paying one tax instead of many. I understand that John has been invited to join the Digital Advisory Group chaired by Rebecca Benneyworth. I encourage the OTS to work through this forum to ensure that HMRC's digital agenda delivers real simplicity.

### **Income tax and NICs review**

The closer alignment of income tax and National Insurance contributions is often called for, but as you set out in your report, this is not a straightforward issue. There are both benefits and challenges to fundamental reform. Your report has made a valuable contribution to the debate on this important issue.

Given the complexity of these issues, I welcome your proposal to conduct two further reviews: one on the impact of moving employee NICs to an annual, cumulative and aggregated basis and another on the reform of employer NICs. The Government will consider your



recommendations and respond in full to your review of income tax and NICs alignment after the publication of these further reviews in the autumn.

### **Different forms of remuneration**

You have often highlighted the disparity between the tax and National Insurance treatment of different forms of remuneration. I would like to draw your attention to a number of relevant measures in this Budget.

First, the Chancellor announced reforms to the rules for termination payments. While it is true that the rules retain some complexity, it is important for the Government to support individuals when they lose their jobs, so the income tax threshold and employee NICs exemption will not be changed. However, we will align employer NICs with the income tax treatment by charging employer NICs on payments above £30,000 where income tax is due. We will tighten the rules to put beyond doubt that if the payment is an existing entitlement, it will be subject to tax and NICs in the normal way. We have also reviewed the other exemptions as you recommended. HMRC will publish a technical consultation on the draft clauses over the summer.

I appreciate that this reform does not go quite as far as you have recommended, but your report encouraged us to look critically at the underlying rules to ensure they remain fit for purpose.

Second, the Chancellor announced changes to the intermediaries legislation, which governs when employment taxes should be paid by





people who work off-payroll through their own limited company. These changes will apply where individuals are working off-payroll for a public sector body. Further details of the reform can be found in a technical note published today by HMRC on the Government's website.

Finally, the Chancellor announced that the Government is considering limiting the range of benefits that attract tax and National Insurance advantages when provided through salary sacrifice arrangements. This will narrow a disparity between the tax and National Insurance treatment of different forms of remuneration.

### **Other OTS recommendations**

Building on the previous package of reforms to expenses and benefits, HMRC will consult on proposals to simplify PAYE settlement agreements (PSAs). This consultation will consider proposals to reduce administrative burdens and clarify the rules for which benefits can and cannot be included within a PSA.

As you know, my officials published a discussion document on the taxation of travel and subsistence in the autumn. However, responses made clear that the current rules are generally well understood and work effectively for the majority of employees. I feel that the benefits of replacing the current system do not outweigh the costs, both in terms of potential revenue lost to the Exchequer and the additional burdens on employers. I am pleased that employers recognised that HMRC's guidance has improved and I feel it is appropriate that employers have time to familiarise themselves with the new guidance.



We will continue to look for improvements to employers' reporting requirements for travel and subsistence, though we will not make further changes at this time.

You may be interested to know that the Government will shortly launch a consultation on how partnerships calculate their tax liabilities. This will look at areas where the taxation of partnerships could be seen as uncertain, as highlighted in your partnerships report.

### **Future reviews**

Along with further work on the impacts of reforming employee and employer NICs, you have suggested that the OTS should review the options to simplify the computation of corporation tax. I agree that this is a complex area that could be simplified over the long term and would benefit from a review. We will agree the Terms of Reference for all of this work in the coming weeks.

To conclude, I would like to thank you and your team for your work. I look forward to meeting with you to discuss your next reviews on the impacts of moving employee NICs to an annual, cumulative and aggregated basis and employer NICs to a payroll basis; and the options to simplify the computation of corporation tax.

A handwritten signature in blue ink, appearing to read "Gauke".

**David Gauke MP**





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**Annex: The Government's response to the OTS's small companies review**

	<b>OTS recommendation</b>	<b>Response</b>
1	OTS develops an outline of a 'Sole Enterprise Personal Assets' (SEPA) vehicle to test its practicability and whether it would deliver the desired personal asset protection in practice.	Accept
2	That the possibility and practicality of a cash basis of accounting being used for the smallest companies is explored.	Accept
3	OTS develops an outline look-through system of sufficient detail to generate proper debate. The would target range of companies that: <ul style="list-style-type: none"> <li>• Do not intend to increase in size;</li> <li>• Are effectively one-person businesses;</li> <li>• Distribute all (or almost all) their profits; and</li> <li>• Have few assets or need for investment funds.</li> </ul> The design should be of sufficient detail to generate proper debate.	Accept
4	That Government seeks to closer align taxable profit with accounting profit following the recommendations of the UK Competitiveness Report, focussing on exploring whether many of the 'sundry tax adjustments' could be eliminated. This could lead to a cash basis under MTD.	Consider
5	The study of a consolidated tax model as part of a longer term strategy for genuine tax simplification for micro companies (and also other micro businesses).	Reject. A turnover-based tax would not account for a business' expenses or profitability, leading to distortions and unfair outcomes between different types of businesses.
6	Seek to enable taxpayers to align filing and payment dates across Government departments wherever possible, e.g. VAT and PAYE, and companies' statutory accounts, annual returns and payment of corporation tax.	Consider



7	Improving VATMOSS system that seeks to simplify EU cross border VAT issues.	Consider
8	Evaluating the feasibility of the establishment of an advance-clearance facility for VAT.	Consider
9	Improves awareness among businesses of the VAT flat-rate and other simplifying schemes.	Accept
10	Simplify expenses claims for small companies by building on the existing flat rate allowances.	Consider
11	Coordinate cross-government regulatory change. The likely departments to be involved are HMRC, HMT, BIS and Companies House and it may be that ABAB can oversee.	Consider
12	OTS will conduct a listening exercise alongside its future reviews to present actions that can be taken forward to improve HMRC's image and relationship with small companies.	Accept
13	OTS is formally involved in the development of Making Tax Digital to ensure simplification issues are considered.	Accept