

Office of
Tax Simplification

Annual report 2016-17:

Challenging tax complexity to help
all users of the tax system

June 2017

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2016

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Foreword

The Office of Tax Simplification (OTS) is the independent adviser to government on simplifying the UK tax system. Since its inception the OTS has made over 450 recommendations with more than half accepted and another quarter under consideration by HMRC.

The OTS was put on a statutory footing last autumn¹, with a new and broader remit and a requirement to report annually “on the performance of its functions”. This is the first annual report which, although formally covering the period to 31 March 2017, also reflects on the work done since establishment - on a temporary non-statutory basis - in July 2010. Future annual reports will be more focused on the year in question.

As far as we are aware, the OTS represents the first endeavour in the world to bring a systematic and thoroughly researched approach to tax simplification, providing

- reports offering practical recommendations in particular areas of the tax system
- analysis that shines a light on challenging structural issues to inform debate
- insight into the implications for tax simplification of societal, economic and business changes

Much has been done in a wide range of areas and, through the way it has conducted its work, the OTS has developed a strong reputation with, and the trust of, government, individuals, businesses, professional advisers and representative bodies.

As independent advisers, strongly connected both within government and with a very wide range of expert tax practitioners and business representatives, the OTS has a unique position from which to highlight structural or apparently intractable issues. These include areas where any significant change has potential to be controversial and so, as a key part of such work, we can expose issues for debate, highlighting options and implications. Examples of this are the two reports on the closer alignment of Income Tax and National Insurance contributions, where there has long been a call to bring these two taxes together. Although clearly a simplification, the second report demonstrated the substantial associated costs and consequences involved.

The work of the OTS is rooted in improving the experience of all who interact with the tax system. We aim to reduce the administrative burden - which is what people actually encounter in practice - as well as simplifying the rules. These are often of equal importance, to taxpayers and HMRC.

The OTS has developed ground-breaking ideas, including its complexity index, put forward ideas that have beneficially affected millions of taxpayers, such as removal of the requirement on employees to file an annual benefits return (the P11D), brought a range of difficult areas into the open for debate and emphasised the importance of simplification being integral to tax policy thinking.

¹ With effect from 28 November 2016: See sections 184-189 Finance Act 2016 and SI 2016/113.

Some of its work includes reviewing areas of the tax system 'at the request of the Chancellor'², such as on simplifying the corporation tax computation. Other projects are initiated internally, for example the Focus paper on the Gig economy.

Looking ahead, the programme is full and challenging, with reviews on the Corporation Tax computation and on some aspects of paper Stamp Duty due to report in the summer, and a review on VAT in the autumn. Other work being considered relates to making tax digital, capital allowances, patient capital and ongoing debate about how the tax system can respond to changes in ways of working and the Gig economy.

As the opportunities and risks of Brexit approach, the economy and ways of working change and as technology and the digitisation of tax administration develop, the involvement of the OTS with its simplification remit, has never been more important. At the same time, it has to be recognised that while the OTS offers advice on simplification, the government will always need to balance ease of administration, economic and political factors, avoidance and other considerations in determining whether to take proposals forward. The role of the OTS is to propose and to stimulate discussion and debate as well as to make specific recommendations.

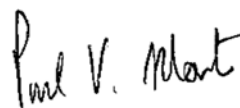
The report on the closer alignment of Income Tax and National Insurance contributions again provides a good example. Some have argued that National Insurance contributions should be merged into an enlarged income tax and at glance this would clearly seem to be simpler. However, the analysis shows that there are many reasons why closer alignment could be a more realistic aim. These derive from the fundamentally different purposes of the two levies, technical aspects, the differences between those who are working and those whose primary source of income is a pension, together with the political realities of achieving reform. So the OTS report highlights the issues and provides a platform for further debate as well as a number of specific proposals which could be taken forward with varying levels of ease or difficulty.

The OTS could not do its work without the support of others, and we are very grateful for the depth and breadth of support and engagement we have consistently received from our wide stakeholder group. This is crucial in enabling us to develop an evidence-based and practical perspective, and to leverage our modest resources - drawn from both the private and public sectors. We look forward to that continuing, and to receiving views on areas we ought to be looking at. Suggestions regarding our future work programme are always particularly welcome.

Finally, we are hugely indebted to John Whiting CBE, who led the Office from the summer of 2010 until March 2017, to the Rt Hon David Gauke MP, Financial Secretary and then Chief Secretary to the Treasury until June 2017, whose enthusiasm and support helped see the OTS established as a statutory part of the tax landscape in the UK, and to all the staff of the OTS past and present.



Angela Knight CBE Chair



Paul Morton Tax Director

² See section 186 Finance Act 2016

1 Who we are - our purpose and aims

1.1 The Office of Tax Simplification (OTS) is the independent adviser to government on simplifying the UK tax system. We are an independent office of HM Treasury (HMT), established under statutory provisions in Finance Act 2016.

1.2 Our remit (in section 185 of that Act) is concerned with:

- the simplification of the law relating to, and administration of, HMRC taxes (including duties and National Insurance contributions), and
- improving the efficiency of the administration of those taxes

1.3 We see this as focusing on two broad areas:

- making the administration of the UK tax system (particularly the “customer experience”) easier for businesses, individuals, advisers and HMRC to deal with, thus reducing administrative burdens, and
- making structural and detailed aspects of the way tax works simpler, not least by making them fit better with changes in the economy and the world of work

1.4 Our output is of two types:

- reviews agreed with and commissioned by the Chancellor (under section 186 of the Act); leading to reports that are laid before Parliament and to which the Chancellor is obliged to respond, and
- other work that we decide to undertake; this covers shorter papers and projects, responses to consultations and general involvement in the wider tax policy development agenda

1.5 All our reports and papers are published on our website, as we see an important feature of our work as being the development of a public debate on tax simplification.

1.6 Simplification is a powerful focus, not least because administrative aspects of tax are what most people come across in practice. So we are keen to advise on simplifying the customer experience of tax as well as on ways to reduce its technical complexity.

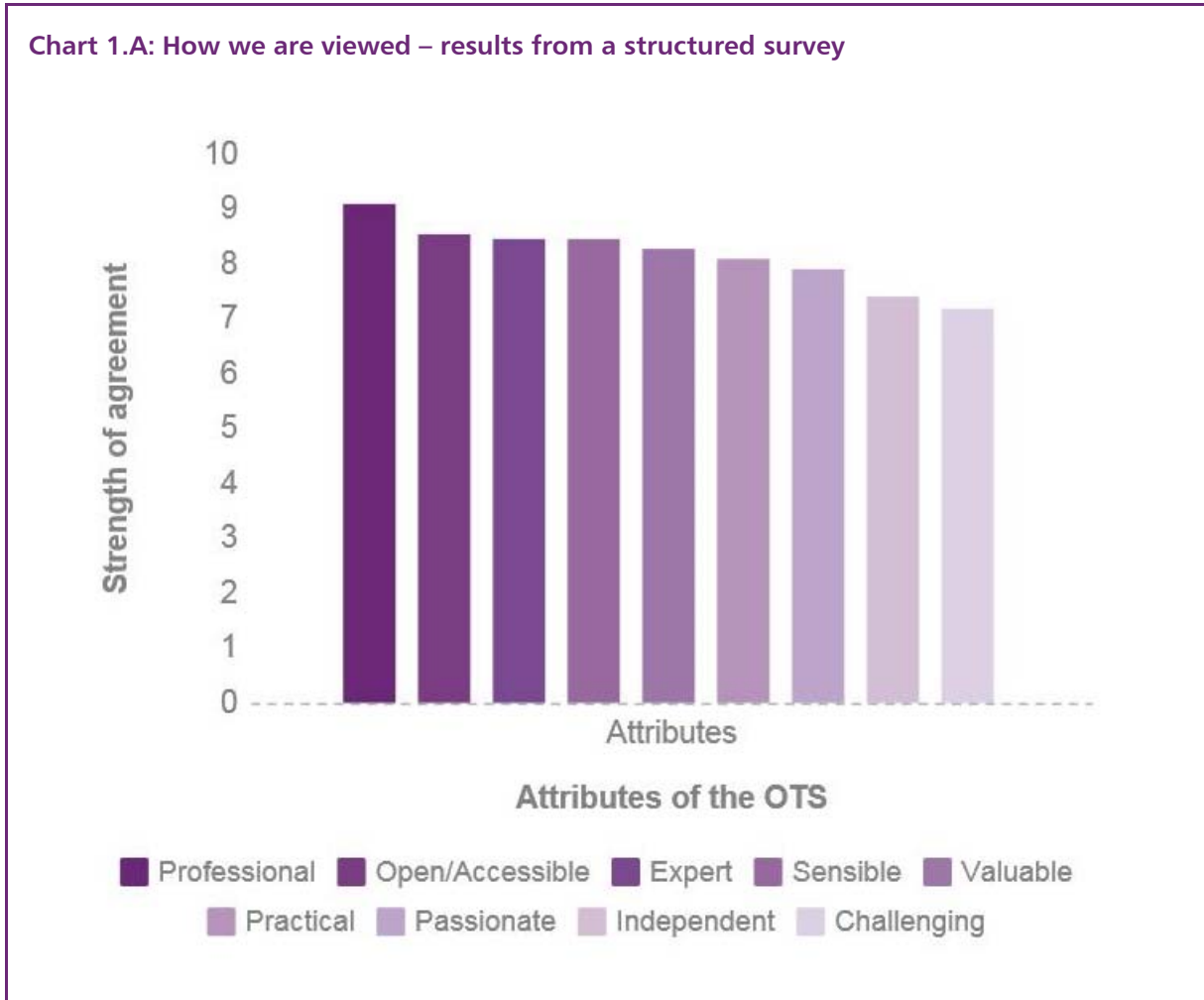
1.7 Equally, as the economy and the wider political context changes, features of the system which may have worked well in the past can become outmoded and need revisiting. One of our main principles for avoiding complexity is that measures need to be kept up to date.

1.8 As independent advisers, strongly connected both within government and with a very wide range of tax practitioners and business representatives, we are uniquely positioned to shine a light on such structural or apparently intractable issues.

1.9 As well as formal reviews of that kind, laid before Parliament, we also take the longer term agenda forward through shorter Focus papers (such as the one we published on the Gig economy in November 2016). Our aim with such work is not normally to recommend ways forward, but rather to promote debate; to highlight the issues as we see them and encourage contributions from our stakeholder group.

1.10 We also play a wider role in public debate in a variety of forums to get simplification higher up the agenda, including giving evidence to various Parliamentary committees, writing in the tax professional and mainstream press, responding to consultations where there is a significant simplification aspect; and contributing to initiatives such as the work by the Institute for Government, Institute for Fiscal Studies and the Chartered Institute of Taxation on Better Budgets.

1.11 In these and other ways the OTS has developed a strong reputation, validated through a structured survey of key stakeholders towards the end of 2016, illustrated in Chart 1.A. We will continue to seek to improve how our projects are chosen, the way we undertake the work and our engagement with the widest possible audience.



How we do business - and why

2

2.1 It has been a key principle of the OTS since 2010 that we seek to develop and sustain open and constructive engagement with all our stakeholders, including HMT and HMRC, to take issues and options out for wide discussion and consultation and to publish all of our work on our website.

2.2 Accordingly, having set a project in motion, we gather views and evidence from all interested parties, including taxpayers, businesses large and small, representative bodies, advisers, think tanks, academics and others, including front-line HMRC staff. In most of our projects we have also gathered ideas and experiences from overseas, by exploiting contacts of our staff, seconding firms and HMT/HMRC.

2.3 We put considerable effort into making sure we gather input from the whole of the UK and from beyond the 'usual suspects' – not that we do not want such bodies to contribute (quite the reverse!) but we see it as crucial that we range as widely as possible. We are strongly committed to improving the extent to which we engage directly with the day to day users of the tax system and ensuring that no one can say that the OTS would not listen to their perspective.

2.4 To help us do that we ensure we are staffed by a mixture of people from public and the private sectors. They contribute from their own experience and their researches whilst with the OTS, and also provide us with many connections to develop further input.

2.5 Although the scope of all the major OTS reports have been agreed with the Chancellor, their content and recommendations are those of the OTS, and we maintain our independent voice at all times. The OTS has a 'critical friend' relationship with HMT and HMRC, and we seek to develop similar relationships with other departments.

Developing ideas and recommendations

2.6 Any change to the tax system will itself, necessarily, temporarily make things more complicated. We have long held that the greatest source of complexity is change, so it is helpful that the Chancellor has decided to focus on one fiscal event a year. Accordingly, we have to ensure our proposals for change are 'worth it', conscious that all changes to the tax system, including simplifying ones, have to be legislated for through Finance Bills following a budget.

2.7 Any remotely significant change will mean altering the amount of tax some people or businesses pay to a degree. So a significant feature of our work is, while focusing on simplification, to flag the often competing calls of simplicity and fairness, highlighting potential 'gainers and losers', and to dispassionately present the key options, impacts and choices.

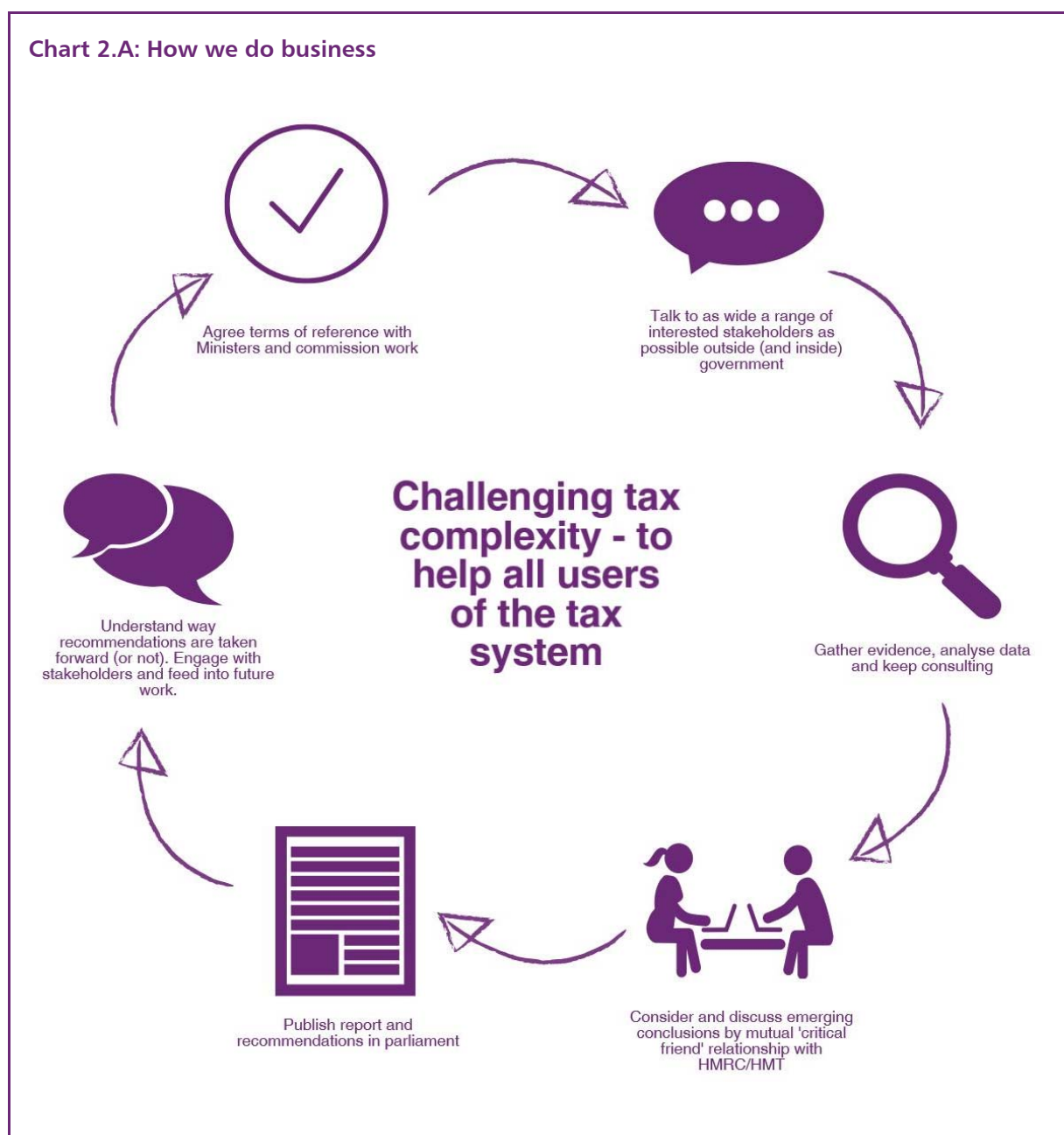
2.8 When the OTS started, in 2010, our mandate was to develop recommendations on a 'revenue neutral' basis, but this proved impractical. We see it as important always to bear revenue implications in mind but not to being rigidly constrained by that, and aim to make it clear where substantial implications of that kind arise. Decisions on our recommendations are of course for ministers and any changes to legislation need to be taken through the appropriate parliamentary process, generally by way of a Finance Bill.

2.9 It is often the OTS's role to establish a base case for changes that will effect simplification and offer clear pointers to the way forward. We consider administrative costs and benefits and

Exchequer costings as far as possible, taking into account transitional issues, risks to the Exchequer and other aspects and make recommendations. It is then for ministers, and HMT and HMRC to consider whether and how, to take the work to the next stage.

2.10 Increasingly we are seeking to ensure simplification considerations are built into the tax policy making and implementation process at an earlier stage. We are ready to contribute to discussions and are able to do so on a confidential basis and now respond to consultations where we can bring a significant simplification angle. We particularly expect to be consulted on the implementation of OTS recommendations where these are taken forward, to ensure that the full reasoning for our recommendations (and the evidence we have gathered) is considered.

2.11 We are also keen to engage with major ongoing programmes of work on which government and HMRC are engaged, such as Making Tax Digital (MTD). In particular, we will offer our perspective on the simplification opportunities opened up by HMRC's work on corporation tax and complex businesses where MTD is not due to be implemented until 2020.



What we have done - and its impact

3

3.1 Between 2010 and 2016, we conducted 14 major projects and produced around 40 reports and papers. The OTS put forward some 450 recommendations of which over half have been accepted, with another quarter still under consideration.

3.2 A complete list of the reviews and other projects we've worked on since the formal establishment of the statutory OTS is set out later in this report. However, it is appropriate that we briefly review the work done in the first six years of our remit when we were developing our ways of working.

3.3 Some of the key successes have been

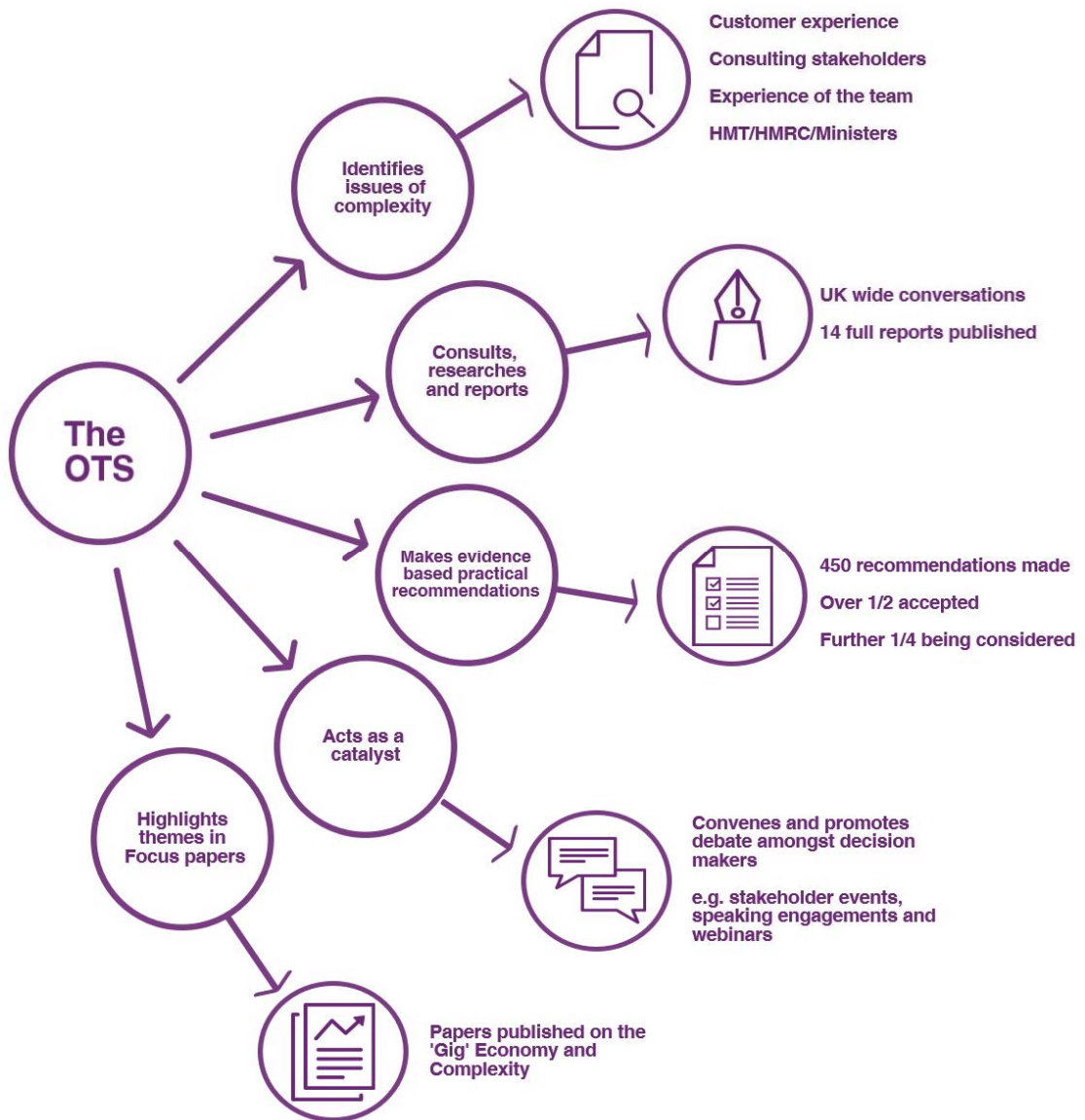
- our first project reviewed 155 of the 1042 reliefs we identified in the tax system, paving the way for the abolition of over 40 and improvements to others; it also showed the value of regular systematic review of reliefs and exemptions, a subject which has since been of interest to the Public Accounts Committee¹
- a cash basis for calculating tax, rather than accruals accounts, for the smallest businesses, now used by over a million of them, and being extended and applied in other areas by HMRC in its current Making Tax Digital plans
- setting in train a series of reforms to largely eliminate P11Ds, including handling tax on employee benefits through the payroll and a trivial benefits exemption
- the abolition of Class 2 NICs
- streamlining reporting of share schemes and harmonising definitions and rules

3.4 Our successes are not just in terms of developing evidence-based, practical recommendations, translated into actions and consequent improvements to the tax system. Our way of working – proactive, wide-ranging evidence gathering, talking to and gathering input from a really representative stakeholder group – has been welcomed as a model of how to consult. We have shown how we value input and through this the OTS has developed a strong reputation with, and the trust of, government, individuals, businesses, professional advisers and representative bodies. This has been validated through a structured survey of key stakeholders towards the end of 2016.

3.5 Another success has been the staffing model, mixing civil servants drawn from HMRC and HMT with private sector staff on secondment or direct hire. In all that we have delivered value for money: we attract a very great deal of quality input and contributions, well beyond what the budget spend might otherwise achieve. In turn, those who contribute see value in their time and input because it is clearly taken account of in our work and recommendations. This becomes something of a virtuous circle and means we are a trusted route for our stakeholders to raise concerns and ideas about the tax system.

¹ See, for example, Chapter 3 of the PAC's 28 November 2016 report on the performance of HMRC in 2015-16 at <https://www.publications.parliament.uk/pa/cm201617/cmselect/cmpubacc/712/712.pdf>

Chart 3.A: The impacts of what we do



4 Looking forward

4.1 The OTS consistently consults on how it is doing and on the future work programme. In the last year this strand of our work has included a stakeholder event in July 2016 attended by 80 people, a structured survey of key stakeholders towards the end of 2016 and a stakeholder round table discussion in February 2017.

4.2 Building on the momentum generated since 2010 and informed by our stakeholder events we intend to pursue a pipeline of work reflecting:

- firstly, projects for the forthcoming year
- secondly, a wider range of projects to consider over the next three years and
- thirdly, identification of areas which should be developed over the longer term

4.3 This pipeline of work will be guided by the principle of applying our resources to the greatest effect which means proposing measures which benefit the greatest number of people on the largest number of occasions. At the same time, however, we will not, of course, ignore an opportunity for a “quick win” which benefits a smaller number of stakeholders but which achieves a useful outcome. We will also consider areas where simplification is clearly necessary even if the numbers affected are smaller and the task is harder, areas where perhaps it is just “the right thing to do”. We will publish our proposed pipeline and update it at least annually.

4.4 The OTS has always focussed as much on the administration of taxes as on the legislative framework and this will continue. The experience of those interacting with the tax system, whether as private individuals, businesses or advisers will continue to inform and motivate our work programme. Perceptions are important as they may determine whether a feature of the tax system works as intended. For businesses, it is vital that tax administration doesn’t unnecessarily inhibit productivity and efficiency. To inform our ongoing work we are particularly interested in hearing from taxpayers about practical challenges they face in dealing with their tax affairs.

4.5 Over the next year we will complete our work in a number of areas:

- our final report on VAT will be delivered in advance of the Autumn Budget
- our final reports on the Corporation Tax Computation and on “paper” Stamp Duty will be published in the summer

4.6 In addition, we will continue to engage with stakeholders on Making Tax Digital and there is likely to be ongoing work on employment status and the Gig economy. We have also reflected on the effect of a range of our earlier recommendations, which has been encouraging, and has provide us with some lessons for the future and contributed to our future agenda.

4.7 Within the one to three year time horizon, we will consider whether there is more to be done in relation to any issues arising from the Corporation Tax report, owner managed businesses and measures designed to support investment and the raising of capital. Other areas for consideration include savings, tax reliefs and the complexity index.

4.8 Our longer term work programme will continue to evolve and develop; we always welcome views and suggestions. The challenges of the digital economy and how new technology might be harnessed to simplify the experience of using the tax system will certainly feature.

Chart 4.A: The OTS in words



5 Projects, Partners and People

Projects

5.1 The OTS has worked on the following reviews requested by ministers in 2016-2017:

- Closer Alignment of Income Tax and NICs review (reports published in March and November 2016)
- Corporation Tax Computation review (progress report and call for evidence published in November 2016 and due to report summer 2017)
- Paper Stamp Duty Review (progress report and call for evidence published in March 2017 and due to report summer 2017)
- VAT Review (progress report and call for evidence published in March 2017 and due to report autumn 2017)

5.2 With the encouragement of Ministers the OTS has also published two reports following up aspects of our Small Company Taxation review (March 2016)

- Sole Enterprise Protected Asset report (November 2016)
- Lookthrough Taxation report (November 2016)

5.3 The OTS has also published

- its first 'Focus' paper, on the Gig economy (November 2016), to highlight the tax issues that we consider it is important are considered alongside other issues, such as employment rights, in debate on this subject
- responses to HMRC consultations on (those marked * stemmed from OTS recommendations):
 - Gift Aid (July 2016)
 - Off-payroll working (September 2016)
 - Making Tax Digital (November 2016)
 - Partnership Taxation* (November 2016)
 - PAYE Settlement Agreement (PSA)* reform (November 2016)
 - Salary Sacrifice (November 2016)
- a response to the joint Institute for Government/CIOT/IFS discussion paper on 'Improving tax policy making' (September 2016), whose report (January 2017) highlighted a number of aspects of our work and growing role

- a Focus paper on Complexity, summarising the work we have done to date on this underpinning aspect of our work, accompanied by updated versions of six papers¹ previously published on this theme; the aim of revisiting the papers and the Focus paper is to stimulate further interest in and contributions to our work in this area

5.4 John Whiting, Paul Morton and David Halsey have also given evidence to Parliamentary committees in this period.

5.5 All of the OTS's reports, papers and submissions are published on our website, where all our material published before the OTS's formal commencement date can also be found.

Partners

5.6 HMT and HMRC are our key partners within government; without their constructive engagement and challenge, and the data that only HMRC's Knowledge Analysis and Intelligence Directorate (which develops the Exchequer costings validated by the Office of Budget Responsibility) can provide, our ability to bring private sector concerns and experience together with public sector perspectives and priorities would be impossible. These relationships operate within a published framework agreement.

5.7 We have a particularly close relationship with ABAB, with its chair being a member of our board and our Tax Director being a member of ABAB.

5.8 We also have active relationships with other departments, such as BEIS and the DWP.

5.9 Outside government, as discussed elsewhere in this report, we consult widely with a wide range of stakeholders both in relation to particular reviews and strategically. Our reports list the organisations, businesses, representative bodies and others we have met and/or received written input from in the course of the project: typically this will be 50-70 meetings. A particularly notable event in this respect during 2016 was our strategy consultation event (with around 80 attendees) on which we reported in September 2016.

5.10 Among these are many leading representative bodies, including AAT, ATT, ACCA, BCC, CBI, CIOT, FSB, IOD, LITRG, ICAEW, ICAS and the LSEW, who also participated in a stakeholder roundtable discussion on our future agenda in February 2017.

¹ These are (with dates first published:

- Length of Legislation (April 2012)
- Tax Thresholds (February 2013)
- Layered Legislation (September 2013)
- Definitions in Tax Legislation (October 2013)
- How to avoid complexity in the tax system (June 2015)
- OTS Complexity index (a number of iterations from 2012 to July 2015)

People

OTS Board

5.11 Legally, the OTS consists of its Board, whose members from 28 November 2016 (when the OTS legislation in Finance Act 2016 came into effect) to 31 March 2017 were



James Bowler
Director General,
Tax and Welfare,
HMT



John Cullinane
Policy and Technical
Director, Chartered
Institute of Taxation



Teresa Graham
Chair of the Administrative
Burdens Advisory Board,
ABAB



Paul Johnson
Director of the
Institute for Fiscal
Studies



Angela Knight CBE
Chair



Paul Morton
Tax Director
(from 1 March 2017)



Kathleen Russ
Head of Tax,
Travers Smith,



Edward Troup
Executive Chair,
HMRC



John Whiting CBE
Tax Director
(until 1 March 2017)

5.12 Angela Knight became chair in January 2016, succeeding The Rt Hon Michael Jack CBE.

5.13 John Whiting has been the Tax Director since the Office started in 2010, stepping down in March 2017.

5.14 Teresa Graham, who has been a member of the Board since 2010, is the OTS's Senior Independent Director.

OTS Team

5.15 The OTS team, or secretariat, is led by David Halsey who succeeded Jeremy Sherwood in January 2016 and acts as secretary to the Board. During the period from 28 November 2016 to 31 March 2017, a total of 14 other people worked for the OTS, either full-time or part-time, who were Angela Brown, Chris Burns, Gary Deans, Marian Drew, John Hampton, Daphna Jowell, Zoe Judd, Nigel Mellor, Andy Richens, Rebecca Seeley Harris, Randeep Sidhu, Olimpia Wojtyczko, Aaron Yamoah and Sue Youngman. Altogether, this was the equivalent of 8.5 full time people.

5.16 Almost 40 different people from the private and public sectors have worked for the OTS at some point during the period since 2010. Throughout this period we have employed a mix of staff on secondment from HMT/HMRC and those hired directly from the private sector, the latter usually on fixed term appointments and almost all part-time. We have also benefitted from some secondees generously provided by private sector firms; we welcomed Ruth Corkin from Grant Thornton from 1 April 2017.

5.17 The OTS's final budget for the year April 2016 to March 2017 was £770,000, of which the pay element was £588,000.

Office of Tax Simplification contacts

This document can be found in full on our website at:

<https://www.gov.uk/government/organisations/office-of-tax-simplification>

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