



ICAEW TAX FACULTY REPRESENTATION

TAXREP 38/10

TAX POLICY MAKING: A NEW APPROACH

Memorandum submitted in September 2010 to HM Treasury and HM Revenue & Customs by the Tax Faculty of the Institute of Chartered Accountants in England and Wales in response to the public discussion document published on 22 June 2010.

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TAX POLICY MAKING: A NEW APPROACH

INTRODUCTION

1. We set out our response to the discussion document *Tax policy making: a new approach* published on 22 June 2010 which outlined a new approach to tax policy making.
2. Many of the principles underpinning this new approach echo similar principles contained in Our Ten Tenets for a Better Tax System which we use as a benchmark to evaluate new tax policies. Our Ten Tenets are summarised in Appendix 1.

WHO WE ARE

3. The Institute operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the Institute provides leadership and practical support to over 132,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The Institute is a founding member of the Global Accounting Alliance with over 775,000 members worldwide.
4. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. The Institute ensures these skills are constantly developed, recognised and valued.
5. The Tax Faculty is the focus for tax within the Institute. It is responsible for technical tax submissions on behalf of the Institute as a whole and it also provides various tax services including the monthly newsletter TAXline to more than 11,000 members of the Institute who pay an additional subscription, and a free weekly newswire.

GENERAL COMMENTS

The proposed approach

6. We welcome the overall approach set out in the discussion document as to how tax policy should be made and kept under review. The approach that has been set out mirrors much of what we have said in many representations submitted to this and previous governments.
7. Our own concerns about the current system are echoed at paragraph 1.3 of the discussion document in that under the current system there are the following concerns:
 - a lack of clear strategy for the tax system;

- consulting too late (and over too tight a timescale) in the policy development cycle;
- the length and complexity of the tax code;
- uncertainty due to the volume and timing of tax changes; and
- inadequate Parliamentary scrutiny of tax legislation.

8. We submitted our pre- Emergency Budget paper to the Government on 2 June 2010 and in the section *Improving Tax Law* we stated:

‘27. The formulation of tax law needs to be improved. The Finance Bill process should adhere to a set timetable and new procedures should be introduced to improve the quality of tax law and provide greater clarity and certainty. We welcome the commitment in the Coalition Agreement to give the public an opportunity to comment on proposed legislation online, and a dedicated ‘public reading day’ within a Bill’s committee stage. We think that the Government should go further and consider using the skills of the House of Lords to improve the detail of tax legislation (accepting that the House of Commons has supremacy on deciding tax policy) and for the Finance Bill Committee to invite bodies such as ICAEW to attend evidence hearings.

28. Consultation – whether formal or informal - should start at an early stage so that government policy objectives can be achieved in a way that minimises any unintended or damaging consequences. Consultation should take place when the policy options and technical details are still being discussed. There may be times when consultation is not practical, eg the need to counter tax avoidance schemes, but this should be the exception rather than the rule.

29. A key principle of taxation is that taxpayers have certainty. In order to ensure that taxpayers have certainty before the start of the tax year, government should commit to introducing a clear timetable for the annual Finance Bill process. Tax changes should be announced in sufficient detail that taxpayers understand their position by the start of the year. If this is not possible, any tax changes should apply prospectively and not retrospectively.’

9. The timetable should provide for ample, rather than adequate, time to debate the draft legislation. Parliament should not be asked or required to pass any Bill with less than full consideration of its content, and debate should be guillotined only in extremis.

10. In our general Commentary on the Emergency Budget announcements we wrote:

‘If these statements of intent are introduced they will amount to the most fundamental reform of tax policymaking in decades. Taken as a whole they should help to restore confidence, stability and certainty into the tax system. The new approach will require much greater discipline and a more considered approach from tax policy-makers. That will be very welcome. The commitment to much earlier and more detailed consultation has also thrown down a challenge to the tax profession. If we want a better tax system we need to put time and effort into effective engagement with tax policy-makers.

11. So we recognise that the new approach to tax policy making presents a challenge not only to government but also to representative bodies such as ICAEW.
12. We believe that stage 1 of the development of tax policy, to set out objectives and identify options (paragraph 2.7) is a particularly important stage. It will enable government to get feedback on the stated objectives and obtain a better understanding of the options that are most likely to achieve those objectives.
13. While we welcome these proposals, the key to their success will be in how they are implemented. The proposals taken as a whole set out a demanding framework that will require a considerable input of time and resources from tax policymakers (and as noted above the tax profession generally) that must be sustained year on year. However, we believe that this will be worth it in the long run if it leads to better tax policymaking.
14. Our concern is that, particularly in the current economic environment with the need to cut costs, sufficient resources will not be made available to do this properly. The processes need to be given time to work and there is a danger that corners may be cut and that the excellent intentions in this document are not translated into a sustained approach on the ground. We believe that this approach needs to be prioritised and must not be allowed to fall by the wayside.

Who should make tax policy?

15. In June 2010 the Tax Law Review Committee (TLRC) published a discussion paper on tax policymaking in the UK. The paper reiterates a number of points that we have made over the years, in particular the relationship between HM Treasury and HMRC in the tax policy making process. Paragraph 1.2 states:

‘However, there is another element in the process of making tax law which also needs to be addressed: the tax policymaking function, currently exercised by HM Treasury and HMRC. Following the reorganisation recommended by Gus O’Donnell in 2004, tax policymaking has been split between HM Treasury and HMRC on the basis that HMT should have lead responsibility and accountability for tax policy, with HMRC being responsible for policy maintenance. Considerable problems with the organisation and operation of the tax policymaking function are being experienced and are identified in this paper. If steps are to be taken to improve the system for making tax law and to make the UK tax system simpler and more effective, then the way in which the tax policymaking function is operated should also be addressed.’

16. We agree. Many of the problems on the ground appear to arise because HMRC are not sufficiently involved at an early stage in tax policy development. This situation needs to be reconsidered and the recommendations in the TLRC paper given further consideration. Although we are reluctant to suggest setting up more committees (not least because they add bureaucracy and administration costs) there may be some merit in establishing a new tax policy advisory committee over and above the Forum of tax professionals (see below) which draws together Government, HM Treasury, HMRC and external experts such as ICAEW.

The Forum of tax professionals

17. We welcome the establishment of the Forum of tax professionals and the appointment of Chris Sanger and Francesca Lagerberg, current Chair and a past Chair respectively of ICAEW Tax Faculty, as two of its founding members.
18. We have no doubt that the members of the Forum will challenge the Government if the new approach set out in the discussion document is not being followed or is not having a demonstrable effect on the predictability, stability and simplification of the UK tax system (see para 4.5 of the discussion document).
19. It is important to stress, however, that the members of the Forum have been invited in a personal capacity and not as representatives of particular bodies or groupings. We believe that there may be some merit in a forum for representative bodies such as the ICAEW to participate directly into tax policymaking at an early stage in its development. Such a forum would provide long-term continuity and commitment from the professional bodies. We have suggested above that consideration should be given to establishing a tax policy advisory committee and it might make sense to combine them or expand the Forum of tax professionals.

COMMENTS ON THE SPECIFIC PROPOSALS THAT UNDERPIN THE NEW APPROACH TO TAX POLICY MAKING

20. Set out below are our various comments on the specific proposals that are summarised in chapter 4.

To promote greater predictability

21. We welcome this approach whereby the Government when embarking on significant areas of reform will set out:
 - its policy objectives;
 - how the reforms will be taken forward, including the approach to consultation; and
 - the proposed timetable for reform.
22. We appreciate that it will take time for the new approach to tax policy-making to be bedded in fully. For the future we propose to test the new approach when responding to consultations.
23. These consultations have all been conducted in accordance with the new approach with the exception of the consultation on restriction of pensions tax relief. This consultation was, however, a special case. We welcome the Government's decision to consider a replacement for the highly complicated and unsatisfactory provisions in the FA 2010 and appreciate that the time allowed for consultation had to be cut short if a policy decision is to be announced in good time to take effect from 6 April 2011.

To promote greater stability

Publish a statement of the government's approach to consultation

24. One of our ten principles is that changes to the tax system should be subject to proper consultation. We therefore welcome the commitment in this paper to improving the consultation process. It is important to remember that to consult is more than just 'to listen to'. Consultation involves taking advice on proposals and ensuring that concerns and views are taken into account properly before any decisions are made. Consultation can take a variety of forms and the precise approach adopted needs to be kept flexible and appropriate to the circumstances.
25. It is important to have a transparent framework of consultation and policy design and one that offers stakeholders a variety of opportunities and times to engage. For example, those who want to see the details before engaging can wait for the draft legislation, but that means that any draft legislation must not be seen as definitive but merely a step along the way to specifying in more detail what the solution may be.
26. Some years ago we suggested that the then recently established Tax Agents and Advisers Group might have a greater role in assisting HMRC and HM Treasury in managing the consultation process and ensuring that consultation was effective and appropriate to the circumstances. We appreciate that this solution may not be perfect and that consultation with stakeholders will often need to be much wider than with the agents and advisers grouping. Nevertheless, we think that the Government should explore with professional bodies such as ICAEW how we can best help to shape the consultation approach based upon the specific circumstances of each case.
27. Tax policy changes will usually be informed by experiences and approaches adopted in other countries. It is entirely right that the UK learns from other countries and many of the consultation documents include international comparisons. In order to aid comparability and to provide consistency, we recommend that where consultation documents include international comparisons, an agreed core list of countries should always be included – even if sometimes a particular core country does not deal with the issue or takes a completely different approach to it. We suggest that the core list should include the USA, Canada, Australia, Ireland, France, Germany and the Netherlands. It would also assist in evaluating international comparisons if those comparisons also included the experiences of taxpayers and their advisers. We would be willing to help in this process by seeking the views and experiences through our international contacts, for example through the Global Accounting Alliance mentioned in paragraph 3.
28. Too often we have been presented with draft legislation that needs amendment but there has been a reluctance on the part of those sponsoring the legislation (whether they be HM Treasury or HMRC officials) to change it. The result is that we end up seeking to try to rectify any deficiencies through guidance. This approach needs to change, not least due to the uncertainty about whether taxpayers can rely on guidance that can be changed at any time. Draft legislation needs to be seen as a stage in the consultation process rather than the end, or nearly the end, of the process. We see this as part of a collaborative process to get the right result.

29. There will be times when draft legislation may need to be amended substantially or completely rewritten – these should not be seen as failures but rather that sometimes this is a necessary outcome of the consultation process that seeks to arrive at the best solution. It would assist those who review draft legislation to see, or review and comment on, instructions given to Parliamentary Counsel and that the latter are encouraged to be involved in this process.

To promote greater stability

Publish a statement of the government's approach to consultation

30. We welcome the proposals set out in paragraphs 2.6 to 2.8 of the discussion document.
31. We believe the three stages outlined in paragraph 2.7 represent the right general approach. Stage 1 should determine what the policy is seeking to achieve and the options to achieve this. Stage 2 will refine the choice of options and determine which is believed to be the best option and how it is to be implemented. At stage 3, detailed legislation will be drafted to put the chosen option into effect.
32. We believe that in most circumstances it should be possible for stage 1 to take place at the time of the annual Budget and for stages 2 and 3 to be carried out between the Budget and the next following Pre Budget Report (PBR). We understand (although we have not seen official confirmation) that the PBR is likely to be scaled down to be an update with new forecasts for economic growth. If that is right then the key point will be to ensure that sufficient time is given for proper consultation. There is some merit in making announcements when they are ready rather than waiting and then publishing them all at the time of the PBR, thus spreading out their publication and avoiding overloading stakeholders. Provided that sufficient time is built in for consultation this process the abolition of a formal PBR should not be a problem.

Consider a new convention to confirm the majority of tax changes at least three months prior to the start of the tax year they come into effect or publication of the Finance Bill in which they will be included

33. The tax year begins in April and the annual Budget normally takes place in March with a Finance Bill generally published within seven or eight days of the Budget announcement. This means that the Finance Bill has usually been published only a few days before the beginning of the immediately following tax year.
34. The time frame proposed of three months before the beginning of the tax year or publication of the Finance Bill will produce a broadly similar result, namely some time at the beginning of January.
35. If the PBR or its replacement (see our comments above) takes place in November, and there has been prior consultation on tax changes, then giving firm guidance as to what are going to be the tax changes in the following tax year by early January looks a reasonable, realistic and achievable target, provided that there are no unexpected surprises when the Finance Bill is published. It would be helpful if draft legislation could also be published by early January.

Take a more strategic approach to tax avoidance and develop a protocol for announcements taking immediate effect outside fiscal events

36. We accept that in exceptional circumstances it may be necessary to announce the introduction of new laws, particularly to counter what is considered to be unacceptable tax avoidance, outside the normal PBR and Budget framework.
37. However, in order to ensure that taxpayers are treated fairly the basic legal principle should be *lex prospicit non respicit* (law looks forward not back).
38. The protocol for announcements should be based on the long established Rees doctrine set out in the late 1970s by Peter Rees (later Lord Rees), the then Chief Secretary to the Treasury. This laid down a protocol to be followed if any government was seeking to end a particular scheme or some exploitation of a provision in the then law.
39. In accordance with the Rees doctrine a government should:
- clearly announce what they were intending to do and the mischief that they were going to put an end to;
 - refer the issue to a special parliamentary committee, the then Tax Reform Committee;
 - immediately publish a draft clause setting out what new law would be introduced to achieve the stated objective; and
 - introduce that clause into the next available Finance Bill for enactment.
40. Peter Rees also added a most important proviso which was that any new legislation should only come into effect from the date of the announcement.
41. We believe that the Rees doctrine still holds good and that as a matter of principle there should never, or almost never, be new legislation which has retrospective effect. We disagreed with the previous Government's statement at the time of the 2004 Pre Budget Report (on 2 December 2004) that threatened to introduce tax avoidance legislation in relation to employment-related schemes that would be backdated, where necessary, to 2 December 2004. Given that the Powers Review has shortened the timescale for re-opening returns to four years where no carelessness was involved, this backstop date is now overdue for a review.

Re-examine the case, and scope, for common commencement and announcement dates in the tax system

42. The consideration in paragraph 2.16 of the discussion document is mainly in relation to fixed start dates for new legislation, but it does also refer to tax changes which are announced at set fiscal events.
43. We believe there would be considerable merit in establishing a fixed time-table for the 'set fiscal events' themselves so that everyone will be aware of the precise date for the Budget and any replacement for the PBR (referred to below as the Autumn Statement) at least twelve months before they take place.
44. There could then be a fixed protocol whereby potential major new tax laws, or major areas for review, could be announced at one Budget with a view to consultation in the run up to the Autumn Statement and the publication of detailed

proposals, and draft legislation, at the time of the Autumn Statement. There could then be a period of further consultation in the run up to the next Budget before the revised draft legislation is published in the Finance Bill.

45. The Finance Bill should be published by 31 March, so that it is available before the start of the financial year (1 April) and the income tax year (6 April).

To promote simplicity

Create an independent Office of Tax Simplification

46. We very much welcome the establishment of the new Office of Tax Simplification which was a key recommendation of the report of Lord Howe 'Making Taxes Simpler' which was launched at our Headquarters, Chartered Accountants' Hall, in July 2008.

47. In his review of the launch of the Lord Howe report in the August 2008 issue of our magazine *TAXline*, our then Tax Faculty Chairman Paul Aplin concluded:

'All too often lip service is paid to the principle of simplification, while practical steps are consigned to the 'too difficult' pile. We have tried – through our ten tenets for a better tax system, through several Hardman lectures, through articles in *TAXline* and through our representational work – to keep the debate running. We believe that Lord Howe's ideas deserve support and, should the OTS become a reality, we would be ready to play a very active role.'

48. We launched our Ten Tenets for a Better Tax System back in 1998 and they are reproduced at Appendix 1. Simplicity is one of the key Tenets for a successful and competitive tax system.

49. Since the publication of the current Tax Policy Making discussion document the government has announced more details of the Office of Tax Simplification, including its terms of reference, and the appointment of an interim Chair, Michael Jack, and Technical Director, John Whiting.

50. We have had discussions with John Whiting and we will be contributing over the next few months to the two initial inquiries, namely reviews of existing tax reliefs and exemptions and small business taxation.

Develop a framework for the introduction of new reliefs

51. We believe that in developing a framework the Government ought to begin with HM Treasury's own *Green Book* which sets out guidance for all government departments and provides a project management tool when developing new policies.

To provide for greater scrutiny

Publish more tax legislation in draft, to allow for pre-legislation scrutiny

52. We have set out above how we believe it would be beneficial to have an agreed time-table for the announcement of tax policy proposals and associated draft legislation. We welcome the publication in draft of proposed clauses for inclusion

in an Autumn 2010 Finance Bill and trust that this sets the right precedent for the future.

Consider how to strengthen the role of Parliament in scrutinising tax legislation

53. The discussion draft considers, in paragraphs 3.9 to 3.11, the role of Parliament in scrutinising draft tax legislation. The question posed in Chapter 4 is by reference to a welcome for 'any consideration by the Treasury Committee of how Parliament's role could be strengthened in relation to scrutiny of tax legislation'.
54. At the moment the Treasury Select Committee conducts hearings into each year's Finance Bill and takes evidence from the ICAEW Tax Faculty amongst others. We welcome the opportunity this gives us to comment on the detailed provisions in each year's Finance Bill and highlight problems where we perceive they exist.
55. However, the Treasury's Committee's hearing takes place within days of the Budget and has tended to focus on the high-level macroeconomic assumptions rather than detailed policy proposals. We understand the rationale for this approach but it limits the opportunity for more considered input about the detailed proposals in the Budget. However, if the proposals in this document are implemented this should provide an opportunity for the Treasury Committee to undertake a more thorough examination of the detailed proposals in the Budget.
56. In the past five years the House of Lords Economic Affairs Committee has also selected a limited number of issues in each year's Finance Bill to take evidence on and to publish a report of its findings. The House of Lords is very mindful that it cannot transgress on the revenue raising function of the House of Commons but its annual Finance Bill reports have been extremely well received and it has been recognised that this is an important additional way in which tax legislation can be properly scrutinised.
57. We believe the Government ought to consider how best to use the resources and expertise in the House of Lords to play a role in scrutinising tax legislation. The House of Lords includes a number of ex Chancellors of the Exchequer and senior Treasury ministers who have considerable expertise and experience. We recognise that the involvement of the House of Lords in considering tax legislation should not compromise the supremacy of the House of Commons, but believe it should be possible to establish suitable protocols so that the role of the House of Lords is limited to improving tax policy and helping to ensure that the government's tax policies work as intended.

To support transparency

Publish more information on costing of tax policies

58. At the time of the Emergency Budget on 22 June 2010 the Government published details of the underlying policy costings to the announcements in *Budget 2010 policy costings* see http://www.hm-treasury.gov.uk/d/junebudget_costings.pdf
59. In the past the Government published as part of the 2010 Budget Red Book the outcomes of Budget Policy Decisions, see Chapter A of the Financial Statement and Budget Report. But that has not included any indication of the underlying calculations that produced the 'effect' of the policy decisions taken in the Budget.

60. We believe that this new publication is a very helpful additional source of information for organisations such as ICAEW to allow us to have greater insight into the fiscal impact of particular policy options and choices.

Improve supporting documentation accompanying tax changes

61. We believe that the supporting documentation could explain in more detail the particular tax changes and the context in which the changes are being made. This would be invaluable to Members of Parliament in enhancing their understanding of the changes they are expected to support.

Consider greater use of sunset clauses for post implementation evaluation

62. In paragraph 3.17 of the discussion document the question is phrased as:

‘the Government will consider greater use of sunset clauses or a trigger for an evaluation in legislation’.

63. We understand the question to be whether there should be a more automatic review of policy measures so that after a certain period of time there is more certainty that a review will be carried out of the effectiveness of the particular policy.

64. We support the need for new policies to be reviewed after a certain period of time, to ensure that they are still delivering the policy objective.

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APPENDIX 1

THE TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. **Statutory:** tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. **Certain:** in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. **Simple:** the tax rules should aim to be simple, understandable and clear in their objectives.
4. **Easy to collect and to calculate:** a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. **Properly targeted:** when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. **Constant:** Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. **Subject to proper consultation:** other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. **Regularly reviewed:** the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. **Fair and reasonable:** the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. **Competitive:** tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see <http://www.icaew.com/index.cfm?route=128518>).