

Treasury Committee

Oral evidence: [Tax after coronavirus](#), HC 664

Tuesday 20 October 2020

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Members present: Mel Stride (Chair); Rushanara Ali; Mr Steve Baker; Harriett Baldwin; Anthony Browne; Felicity Buchan; Ms Angela Eagle; Siobhain McDonagh; Alison Thewliss.

Questions 205 - 274

Witnesses

I: Professor Judith Freedman CBE, Professor of Taxation Law and Policy, Faculty of Law, University of Oxford; Bill Dodwell, Tax Director, Office of Tax Simplification; Derek Cribb, Interim CEO, Association of Independent Professionals and the Self-Employed; Andrew Titchener, Head of Tax Policy, Confederation of British Industry.

Examination of witnesses

Witnesses: Professor Judith Freedman CBE, Bill Dodwell, Derek Cribb and Andrew Titchener.

Q205 **Chair:** Good morning and welcome to the Treasury Select Committee's latest inquiry into tax after coronavirus. Today we are specifically going to be looking at employment taxes. I am delighted to be joined by a very strong panel of four. I am going to ask each of them to introduce themselves for the public record.

Bill Dodwell: I am Bill Dodwell. I am the tax director of the Office of Tax Simplification.

Professor Freedman: I am Judith Freedman. I am professor of tax law and policy at Oxford University.

Derek Cribb: Good morning, everybody. I am Derek Cribb. I am the interim chief executive of the Association of Independent Professionals and the Self-Employed.

Andrew Titchener: Good morning. I am Andrew Titchener. I am head of tax policy for the Confederation of British Industry.

Q206 **Chair:** Thank you, everybody, for joining us this morning. We really value your time. We are going to handle the questions in sequence, member handing over to member in turn. Generally, questions will be put specifically to one or more of you, but if you are not brought in on a particular question please do not hesitate to raise your hand. I will endeavour to make sure that you get in to make your point on that particular question.

I am going to start with a question to Andrew. We know that taxes are almost inevitably going to have to rise at some point in the future, given the amount that we have been borrowing, and that income tax and national insurance are two of the highest-yielding of those taxes. What damage to the economy and jobs do you think raising income tax or national insurance would create?

Andrew Titchener: It has been said by other witnesses in previous sessions, and we would agree, that the time for any tax rises is not now. We are still in a crisis phase at the moment. We would see any rise as being considered quite a bit into the future. In terms of damage, looking at it from an employer's perspective, when we are thinking about tax and paying for the crisis, the important thing is that we need to encourage business to invest and create jobs. Tax rises that increase the cost of employing someone are difficult because they dampen that job creation. At the same time, tax rises on business that deter investment in capital and suchlike are not good either.

Another way to raise money to pay down the debt, if we look beyond headline tax rises, is to get businesses growing, investing and creating



jobs. This creates employment and profits, which ultimately feed into a higher tax base.

Q207 **Chair:** I agree with that. Going back to the tax question and the damage done, thinking of your members at the CBI, are you saying that it will be better to raise corporation tax, and raise £5 billion or £10 billion a year doing that, than to raise an equivalent amount through employment taxes?

Andrew Titchener: I am not able to comment on the precise mix. From a CBI perspective, looking at one particular tax in isolation is not really something that we think would be sensible. You need to look at the whole tax base, and think about a balanced position of tax rises across all the different areas and how that balance works. The key thing for us is that that balance should be done in such a way that it encourages business to invest and allows business to grow.

Q208 **Chair:** Can I quickly ask you about corporation tax? This is one of the bigger taxes that are in play here. I get the sense that businesses feel that that tax is pretty internationally competitive, and that if the Chancellor were to hike that tax in the future there would not be a lot of squealing around that. Is that your sense?

Andrew Titchener: Any rise in the headline rate of corporation tax impacts business investment decisions. At the moment, what is important for businesses is not just the headline rate, because the headline rate does not always reflect the tax that is actually paid. Things that are important for business are reliefs and incentives to invest in the UK beyond just the headline rate. Looking at the headline rate in isolation is not necessarily the thing. It is about the whole tax environment for business in the UK.

Q209 **Chair:** Derek, on the issue of the self-employed, if they were to bear more tax, where do you think the self-employed would be most comfortable bearing more tax?

Derek Cribb: If I am entirely honest, I am pretty sure they would not be comfortable with any tax rises. Being self-employed, you tend to have significantly fewer reserves than some of the larger organisations. The idea of an increase in taxes, whether that is corporation tax, NICs or dividend tax, would be very difficult to bear after what has been a pretty tough six months, and ultimately 12 months, before we come out of any form of lockdown. If there were to be a rise in corporation tax, it would be good to see a differential rate to support the smaller, more entrepreneurial businesses for the self-employed. That has been done in the past and we would look to it again as a way of supporting those who are effectively least able to get through this crisis.

Beyond that, we saw suggestions in the Mirrlees report many years ago, looking at VAT on financial services as a way to keep the tax burden down on the rest of industry.



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Chair: That is applying VAT to them.

Derek Cribb: Yes. The other one, which has been touched on to a certain extent, is on the very large global business. There is a view that perhaps the global businesses, or very substantial businesses in the UK, that pay hardly any tax might be a preferential target to the small entrepreneurs that are trying to get the British economy back on line.

Chair: If you are looking at the Amazons, Googles and Facebooks, digital services taxes and changing the international tax architecture to tax them more on the basis of where the value is created, in this case the United Kingdom, that does not leave a huge amount. You are talking about £1 billion here or there. It is not going to suddenly transform our ability to spare others taxation rises.

Derek Cribb: It is part of a package of wider measures. It is about getting the balance right and reinforcing the support for the smaller business, the self-employed and the entrepreneurial element.

Q210 **Chair:** Derek, you have given us examples of other people who could pay taxes, or taxes that might be reduced on smaller companies, such as corporation tax. If the self-employed are to bear a bit more tax going forward, and it looks everybody is going to have to, one way or another, where is that extra burden best to fall? Where is the least uncomfortable place that it might arrive for the self-employed? You know it is going to happen, and the Chancellor is sitting in front of you and he says, "It is your choice, Derek. What option do you want to press the button on?" Which one do you recommend?

Derek Cribb: We have to see what the balance of taxes is. For the self-employed you have a complex matrix, covering PAYE, dividend tax and corporation tax. I would not want to say any one of those is where you should put extra measures for taxation.

Q211 **Chair:** Let me rephrase it. You are not going to be drawn into suggesting areas for tax rises. Where would you strongly advise the Chancellor not to go with the tax increase for the self-employed?

Derek Cribb: I will come back to the point that these are the people who have the lowest assets and the least ability to get through. Taxing them as they come out of coronavirus is not the right way to go. Many of them have already had to shut up shop. They will not be able to survive if they have to bear more tax. Leave it for a few years down the line and revisit it.

Q212 **Chair:** We are working on that assumption. We are all agreed that it would be very ill advised to whack up taxes in the short term. The question relates to a couple of years down the line. Is there anywhere you think the Chancellor should definitely not apply any further taxation to the self-employed, any particular element or aspect of their tax?

Derek Cribb: I am sorry, but I am not going to be drawn on suggestions.



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Q213 **Chair:** Okay, thank you. Bill, for income tax and national insurance, can you talk us through what you see the arguments being around the benefits, or otherwise, of raising rates rather than thresholds? The Chancellor is sitting there and he has that choice. What goes through his mind in terms of the swings and roundabouts of taking either option?

Bill Dodwell: That is not directly a topic that the Office of Tax Simplification is accustomed to, because we do not normally talk about rates specifically. The general point to be made on that is that rates do spread things more broadly. Over the last decade, we have seen the personal allowance rise and we have recently seen the equivalent for national insurance rise. If you lift thresholds, you take some people out of the tax or national insurance net, but at the same time because of the strong link with benefits people at the bottom of the distribution do not necessarily get the benefit from all that.

The benefit mainly goes to people in the middle of the distribution, not at the top, because it is withdrawn. The middle is where it works out. I suspect that is a question that the Chancellor will face. Putting up rates is a simpler thing, although we have not seen a rise in basic rate income tax in living memory. It has just come down, in our time. That would be a fairly unusual measure. Nonetheless, it raises a lot of money, because it is very broadly spread.

Q214 **Chair:** Judith, switching to pension tax reliefs, would it be better on balance to look at pension tax reliefs as a way of raising money rather than income tax and national insurance, if the focus is on jobs and growing the economy? What would your view be of that, please?

Professor Freedman: I do not see them as alternatives. It has to be a package, as people have said. I agree with other witnesses that looking at rates in isolation does not work well. You have to look at broadening the base as well. If you are looking at broadening the base, people in receipt of pensions should be within your purview because they are not paying any national insurance on those pensions. There is scope to have a look at that section of the community. Speaking as one of them, I do not think it will be popular, but it probably should be done

Chair: As that round of questions has aptly demonstrated, any suggestion of tax rises anywhere is unfortunately never going to be popular, but these are difficult choices that will have to be grasped at some point.

Q215 **Mr Baker:** Derek, I hope you will not mind me saying that you missed an opportunity to put the boot into the Government. Is it not the case that some of the people you represent are going to be dismayed if they end up paying higher taxes when they did not get a bail-out because they were just over the £50,000 limit?

Derek Cribb: There are whole host of reasons why people did not get a bail-out. The £50,000 limit is one of them. Those who are recently self-employed have not had the opportunity to put in a tax return; they



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are excluded. People who pay themselves predominately by dividends got nothing out of the furlough scheme. Effectively, one in three of the self-employed population have seen no support whatsoever. As you say, the idea of them having to pay tax to fill the coffers that have been emptied out into other people's pockets is a little challenging to sell to our members.

You can add to that the latest tier 3 lockdown rules, which completely exclude the self-employed from any support whatsoever. When we talk about tax rises on people who have had no support and minimal assets to see them through this crisis, it becomes quite a difficult sell to our members and the self-employed as a whole.

Q216 **Mr Baker:** Is that as far as you want to go? Eventually, I am sure Ministers will give in and come to see us, so we can ask them questions. Is that as far as you want to go in what you want us to put to Ministers on your behalf?

Derek Cribb: That will do for now. I am sure more will come up in the next hour or two.

Q217 **Mr Baker:** Andrew Titchener, in your written evidence you speculated about employers allowing people to work from home outside the United Kingdom. Should the Government try to stop jobs being offshored or is it no business of Government's where people work?

Andrew Titchener: It is not for me to answer whether the Government should interfere with where people work. The point we were making in the written evidence is that the tax system potentially has to adapt to that. I should stress that, at this point, this is really rather anecdotal evidence. It is too early to say whether this trend will continue and grow. Anecdotes from our members suggest that, as a result of the crisis and people working from home where they can, more have said, "I have a laptop and an internet connection, so why can I not just work from anywhere?" There are not just issues with tax; there are issues with employment law and other areas.

Having seen and been involved with the CBI efforts around the reform of the international corporate tax system, and having seen the difficulties encountered there, the point we were making in the written evidence is that, if this trend is to continue, to avoid the real difficulties that have been encountered with the corporate tax system, it might be sensible to start thinking about how the labour tax system adapts to it now rather than in 10 years' time, when this has all happened.

Q218 **Mr Baker:** Can I press you to elaborate on what you think the tax challenges are? Back when I was a freelancer, I would occasionally go to a drop zone in Spain and do some programming. It never occurred to me to think that anyone would ever think that it was a problem; I was ordinarily resident in the UK. What is it you are really worried about? Are you worried about jobs going offshore? I cannot imagine that you are



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worried about people popping to their holiday home in France and doing some work from there.

Andrew Titchener: No. It is not a broad point about jobs offshoring. There are a couple of issues that we have identified already. More may come up as time goes on. One is the corporation issue around establishments and corporate residence. Are those people creating a taxable presence for their employer, where perhaps their employer did not have one before? That is an issue that has been managed, and there has been some welcome guidance on that as part of the pandemic guidance. The OECD issued some guidance saying that should not necessarily be the case.

On the individual side, there are issues of individual tax residence, individual payrolls and where they should be on a payroll, depending on where they are working, if they are popping in and out of countries. It will depend on how mobile people become. It may be that you get a lot of people fixed in one location, say in a European country, doing a lot of work for a UK business, on a more frequent basis than occurs at the moment.

There is the bit about individual residence. Where are they; where are they resident; what payroll should they be on; what taxes and social securities should they be subject to? You then move into a realm where perhaps, if you have a much greater dispersed workforce in a large multinational organisation, they could be performing duties in places all over the world and a mix of duties in respect of lots of different countries. I am sure that this happens to some degree already in some respect, but there is the potential for this to increase to the point where it becomes a fundamental issue to address in labour taxation. I am certainly not suggesting that it is an immediate problem that we must fix now, but we can foresee it coming over the horizon in years to come.

Q219 **Mr Baker:** Professor Freedman, do you foresee difficulties in the future on this point, or is it not something that you have looked at yet?

Professor Freedman: It is probably too soon to tell whether that would be a real change of pattern, because once people are allowed to come back and see their families presumably that is what they will do. I would not have put this as the highest problem.

Bill Dodwell: There is a proliferation of this, and this happened before the pandemic. You see various platforms offering services as well as selling goods. All the focus has probably been on goods, holiday homes and that sort of stuff, but we should not forget that you are now seeing platforms supplying services. There is a real question for tax authorities generally on how you enforce taxes in this situation. You have to define what the base is; you have to get information and then lead to income tax.



The OECD is doing some work on that, and I am sure that it will need to be accelerated, for the reasons Andrew has given more generally. It is not just about employers; it is about freelancers being able to provide freelance activities from around the world. The question is then whether you should tax where the services are rendered as opposed to where they are performed and how you deal with the enforcement question.

Q220 Mr Baker: Thank you. That brings us on to broader issues. How do you think changes in the labour market after coronavirus will change the way that taxation should be applied, if at all? Are you expecting a sufficient return to normal, such that we do not need to fundamentally change the tax system, or do you think the tax system will have to change?

Professor Freedman: We are already seeing changes in work and an increase in the gig economy. The pandemic is probably going to increase that and increase platform working, as Bill has said. Those are the areas that I think will change, but it is far too soon to say how much of that will be pandemic-induced and how much it would be a continuation of the trends we have seen already. We need to tackle the position of people who are working for more than one engager or working through platforms. Those things needed to be looked at before the pandemic, and we now need to look at them even more urgently.

Q221 Mr Baker: You have provoked me to ask you about IR35 because you have just made the point about more than one engager. What are we to do for people who are on a two-year contract on a project for a single engager? What are we to do for them as they work from home?

Professor Freedman: I think we might be coming on to that. We should probably be treating them much as anyone else working from home. The fact that they are working from home does not make a difference to the arguments around that, and I do not think IR35 is the solution.

Derek Cribb: A lot of this comes down to trying to understand the employment situation of somebody, whether they are self-employed, a worker, an employee or whatever it might be. At the moment, the boundary seems incredibly unclear despite the work of the Taylor review, which has never really been seen through. Before we start worrying about IR35 or any other variant or taxation, let us try to understand the employment status.

The problem with IR35 is that you effectively get pseudo-employment, with no employment rights, quite often retrospectively. How you are supposed to manage your business or self-employment while you have that level of uncertainty is beyond me. That is a comment I would make about the wider taxation system, particularly as it applies to the self-employed. Unless you know what your tax situation is, you do not know what your charging rate or your engagement contract should be. It is all about getting a huge amount of clarity up front as you are engaging in new projects.



Mr Baker: Thank you. I must draw stumps. Finally, I will just give any member of the panel who wants it an opportunity to argue that homeworking is a risk to the UK tax base. Has anybody taken that position? No.

Q222 **Anthony Browne:** I should declare at the outset that I have been self-employed for a few years. I have been a director and am an existing shareholder in a company called Coconut, which provides banking services to the self-employed.

My question is about the level playing field in taxation between the self-employed and the employed, picking up on some of the points that have been raised. The self-employed are taxed less heavily than the employed, particularly because of employer national insurance contributions. Not going into the arguments we have just heard about whether they should have more support during the lockdown, is there a rationale on an ongoing basis for the self-employed to be taxed differentially from the employed? How much should that difference be? Should there be more of a level playing field between the employed and the self-employed when it comes to taxation?

Professor Freedman: I do not think there is any principle at all on which the self-employed should be taxed at a lower rate than employees. There is some small difference in rights to benefits, which accounts for about a 1% difference, around parental leave and jobseeker's allowance. Beyond that, there is no good rationale. The rationale usually used is to encourage entrepreneurship and so on, all of which is very important. We are going to need to encourage entrepreneurship after this pandemic. However, doing that through a blanket relief to all self-employed, some of whom are not particularly entrepreneurial, does not seem to be a good way of using scarce resources.

I would rather see any resources we have to encourage entrepreneurship used in a better targeted way. As far as the tax system is concerned, the ideal is to be as neutral as possible between different legal forms of working, because that would then not distort the market. Both the engagers and the engaged would decide how best to organise their businesses without having to take tax into account. That would be far better commercially and would be good for the economy.¹

Q223 **Anthony Browne:** Is there not an argument that the self-employed take on more risk and that should be reflected in the tax system?

Professor Freedman: The tax system is a very poor vehicle for reflecting that risk, because some self-employed take on risk, but some take on very little or no risk. Therefore, if you use the risk argument, it does not work well. Some employees are in very risky and precarious employment. Risk is not related to the amount of tax being paid under

¹ *Note by witness:* I am not saying tax should be dealt with in isolation from employment law. We always need to look at things holistically, but it is not the case that one simple definition can answer a range of disparate problems.



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the current system. It would be impossible to devise a system that would properly reflect risk within the tax system. There are other ways of assisting people to take risks. Tax is a pretty crude instrument for doing that.

Q224 Anthony Browne: Derek, do you think there is a sustainable reason for different levels of taxation for the self-employed and the employed?

Derek Cribb: Unsurprisingly, I am going to disagree with Judith on a few of these points; I agree on others. Tax is a very blunt system and blunt implement for differentiating between types of risk, in terms of your business. Sadly, it is the only one we have. Yes, there is a differential that needs to be there. We do need to encourage the entrepreneurialism.

There is also a premise here that the self-employed want the same support and safety nets as employed people have. I am not sure that is always the case. A large number of the self-employed are more independently-minded, risk-taking and entrepreneurial. That does not mean they never need support. Coming back to the coronavirus and support packages, we need to look outside the normal economic 10-year cycle, or whatever it might be, where I do not think most of the self-employed would look for support from the Government. Coronavirus is more of a one-in-100-year event, and with that everybody needs a bit of extra support. We need to be careful about differentiating between the two levels.

In terms of the UK workforce, we have a pretty good balance between the self-employed and the employed. The World Economic Forum a few years ago ranked us about fifth for the most efficient balance in that workforce. If you start degrading the gap, small as it is, to an even smaller gap between employment and self-employment, you would start distorting that flexible workforce. That flexible workforce is really key to the UK being able to get out of the economic crisis we find ourselves in with coronavirus.

Q225 Anthony Browne: Can I press you on that point? Do you think the differential, which is quite large because of the employer national insurance contributions, is the right size? Judith Freedman made the point that the taxable benefits you get from employer NICs are minimal, just 1% of the actual cost to the Treasury. Do you think the gap is the right size? How can you justify it being that size?

Derek Cribb: If you look at the tax collected from the employee or the self-employed person, the differentials between employment and self-employment are quite small. In some cases, you get more from the self-employed people than those in employment. The difference is not in what the employee or the contractor is paying. Quite often, the difference is in the employer's NI. When it comes down to it, that really is the differential.



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You might argue that, if there was some sort of engager's levy that people using contractors had, that might feed down to the contractor anyway. But, if I was looking to close the gap, I would look at some contribution from those who engage contractors, as almost a proxy for the employer's NI, rather than trying to increase tax and NI on the contractor.

Q226 Anthony Browne: Andrew, you represent the employers. How do they feel about the playing field between the employed and the self-employed? Should it be more level or is it about right?

Andrew Titchener: Derek has mentioned a couple of things about employer's NIC being the main tax difference, in terms of the cost of engaging somebody for an employer, and the flexibility of the workforce. In the end, the differential in cost is taken into account when employers are making decisions, but there are a huge range of reasons why an employer would engage with someone as a contractor or as an employee, around the type of work you are doing, the sector you are in and the sort of project you are doing.

One of the other things is certainty. If employers are trying to decide what they need for their workforce, whether someone permanent or a contractor, the way that employment status is currently quite difficult to manage and come to a conclusion on is probably as big a thing, if not bigger, than the tax. There is a risk to the employer, in that they cannot be sure in certain cases whether they have got the status right for the person they are engaging with. The fact that they have to pay people to help them decide that adds to the overall cost of engaging somebody.

Tax is one thing and there is a differential there, but there are a lot of other factors to do with employment and self-employment, around the status, that impact employers' decisions.

Q227 Anthony Browne: We will come to some of that later. Bill, you are at the Office of Tax Simplification. The easiest solution would be to merge NI and income tax. That is a question we will come to later; my question is not about that. Do you think there should be a level playing field between the employed and self-employed?

Bill Dodwell: Economically, yes, there should be a much closer alignment of overall tax burden. You have to bear in mind that it is not easy to work out the best way to get there. As you said, we have employer's and employee's national insurance, and then income tax taken from an employee. A self-employed person pays self-employed national insurance, albeit at a lower rate, and income tax. Of course, a great many freelancers provide their services via a company. Work from the Institute for Fiscal Studies and others has demonstrated that people in that category can use the flexibility of a company to smooth out their tax rates and, over time, end up with substantially lower rates than everyone else through all that.



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There is definitely a case for looking at evening up that burden of taxation, and you will have to find different ways of doing it. I specifically agree with the point made by Andrew that we do not easily know who is a self-employed person versus an employed person. Some of the employed are pretty obvious, but we need a better statutory test. I do not just mean taking the existing, muddled case law and trying to turn that into statute. I would suggest that Parliament needs to pick this up and ask who exactly we want to be treated as self-employed. Once we have worked out the answer to that, and we would need to take a lot of evidence, we would then need to come up with a statutory test. That way, you would have everybody in the whole mix knowing which side of the line they rested on.

Q228 Anthony Browne: We all agree that we need clarity on that. Professor Freedman, I want to pick up on a point that you made. You said that there are better ways of reflecting risk outside the tax system; it is too blunt. How would you do that to reward the self-employed who are taking risks?

Professor Freedman: It would have to be by targeted grants and more incentives for investments. We are very poor in giving incentives for investments in the UK. That is one of the areas where we are least competitive, so that might be a way to do it. The annual investment allowance has been very helpful. The increased annual investment allowance might be a way forward, keeping that high.

Q229 Ms Eagle: I am going to ask some questions about the Taylor review in a minute, which really forms a background to the issues we are dealing with of differential employment statuses. Professor Freedman, how can we reform the incentives in the tax system and employment law to facilitate free treatment and protect the tax base? With this hotchpotch we have ended up with, we are not achieving any of that.

Professor Freedman: I agree with other witnesses that we must look at the question of people incorporating, the employed and the self-employed, which is a spectrum, as one. We must try to achieve greater certainty for people. The current off-payroll rules are going to something of a nightmare for engagers. I agree with Bill that we need to consider what we are trying to achieve. Who do we want to tax in a certain way, and does it necessarily mean we have to tax people on the basis of their employment status?

We might need to look outside the box and move away from employment status as the test of how we want to tax people. Taylor said that we should be aligning the treatment of the employed and self-employed, which is a good idea. He also went on to say that we should have a definition that is the same for tax and employment law. One problem in reforming this area is that trying to get a test that is the same for tax and employment law is trying to kill too many birds with one stone, because employment law and tax have very different objectives. Focusing on tax and having a definition, as Bill said, that looks at what we need to do



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from a tax point of view, who we want to tax through collection at source and who it is practical to tax through collection at source, without worrying about whether they are employed or self-employed, might be the way forward.

Q230 Ms Eagle: The coronavirus crisis has shown up how unfit the current system is, not least because so many people were excluded because of the way they were taxed and their employment status as either self-employed or not. You are in favour of starting from a tax point of view, rather than an employment protection point of view, to sort this mess out. People talk about flexibility in the labour market, but the Institute for Fiscal Studies and the TUC have both shown that those who are on zero hours and fragmented hours contracts are more likely to be young, black and minority ethnic, and low paid. There is a huge unfairness and exploitation going on in employment law at this end.

Professor Freedman: Yes. It depends on what you mean by flexibility, but it is perfectly possible to achieve flexibility through an employment contract. There is a myth that you cannot have flexible employment; you can. If you are trying to solve the very real problems of employment law and tax law with one definition, you are going to be very disappointed because those problems are different. We need to protect the vulnerable and we need regulation to do that. We then need to decide how it is most practical and equitable to tax people. They are two separate issues.

Q231 Ms Eagle: There are incentives to claim that you are self-employed, or for your employer to claim that you are self-employed, most notoriously on building sites, but spreading to other areas of the country, because you can end up with a much lower and more flexible tax treatment. Would you agree that at the heart of reform in this area is actually being more neutral in tax treatments based on the kind of employment you have, whether it is self-employed or employee, however you want to categorise that in law?

Professor Freedman: Absolutely, the aim should be to be as neutral as possible, from a tax point of view, so that there is not a tax incentive that will exacerbate the employment law incentive to make people self-employed, or supposedly self-employed. At the moment, both sets of incentives move in the same way and they reinforce each other. For an engager, all the incentives are moving towards them trying not to take on employees. If that were to change so that the tax was neutral, we could look more clearly at the employment law to see whether someone should have certain protections.

Q232 Ms Eagle: You think that you do the tax first and then the employment law.

Professor Freedman: You do them in parallel. Taylor had various ideas that should be looked at and possibly implemented and discussed with employment lawyers. I am not saying that you should not look at them together; they have to fit together. You should look at the different



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problems and objectives, and possibly have different treatments for them. The idea that the case law is only about tax and employment is also incorrect. There are many cases about vicarious liability and tort, for example. If you start trying to mess around with the definition for all purposes, you are going to have to take into account so many areas of law that I do not think you can do that. You have to tackle the objectives that you are trying to deal with.

Q233 Ms Eagle: Derek Cribb, the Taylor review was commissioned in 2016 and published in July 2017, with 53 recommendations. There was a Government response, but there has been a crushing silence and no real progress since then. What should be done with the Taylor recommendations?

Derek Cribb: We broadly support the Taylor report. There was some really good content in it. Frankly, we were a little surprised that more progress has not been made. I am not sure I am the person who can say why progress has not been made. There are probably better people in Westminster who can answer that.

Ms Eagle: We can all speculate.

Derek Cribb: I would like to pick up a couple of points from Judith's answer. It is important that we define exactly what employment and self-employment is, and there has to be a strong connection to how tax works from that. I am not convinced that that can be done in parallel. They are very complex issues, around the legal definition and how tax comes into play. Two separate exercises doing that in parallel will almost certainly not connect at the end. From our perspective, let us get the definition in there, if we can, and from there see if we can harmonise tax treatment to employment status. For me, that is the key point that comes out of the Taylor report.

Q234 Ms Eagle: Would your way of doing things not maintain the incredible complexity and not give us a chance for more fundamental reform, which would give people much more certainty? This is what you were arguing for earlier, after all.

Derek Cribb: Certainty is incredibly important, but it is not something you can take a shortcut to. There needs to be a wholesale review. We have mentioned IR35, and I am sure we will come to it again. We have a piece of legislation there that is so clear that HMRC, in trying to enforce it, seems to lose more cases than it wins, and a piece of legislation that, from what I understand, is potentially fundamentally flawed and may need more primary legislation to make it viable to come in in 2021. In tweaking that in the next Finance Bill, who knows whether further issues will come out?

Q235 Ms Eagle: You are arguing for simplification. Bill Dodwell, you do tax simplification. Do you see the approach to simplifying and standardising the tax rules around employment status as a way of dealing with a great deal of complexity and giving people more certainty?



Bill Dodwell: It is important that we devise a better test for self-employment so that we know who is an employee for tax purposes, and who is a self-employed person for tax purposes.

Q236 **Ms Eagle:** Should people on building sites be deemed as employed, rather than self-employed, when it is fairly obvious that they report to the same site and work for the same people? If it looks like employment, should it be deemed to be employment?

Bill Dodwell: If it looks like employment, it ought to be recognised as such. I am not sure I entirely agree with you. My personal experience of working on a building site rather suggested that it is very possible to be a self-employed person under the current law in that category. For that sector we also have a withholding tax, to ensure compliance through that, under the Construction Industry Scheme.

I would go back to the point that Professor Freedman and others have made. The bigger the tax and national insurance difference you have between the various ways in which you provide labour and services, the more economic encouragement there is to shift into the lower-taxed version of it. If you did not have that difference, people would end up working the way they wanted to work, untainted or un-pushed into it, if you like, by tax.

Q237 **Chair:** Can I just pick up on that discussion? Derek, if we had a move to a tax neutral situation, as between the different structures of employment, which might mean more tax for the self-employed, on the basis that that could remove at one stroke IR35 and all the problems around that, would that not be a price worth paying?

Derek Cribb: We really need to keep the incentive there for people to be entrepreneurial and self-employed, and less reliant on Government support. It is important to remember that the burdens that come with self-employment are considerable. It does not matter whether you are incorporated. The level of administration and extra insurances that come with that, and the fact that your personal assets are at risk, are all effective economic costs that come with being self-employed. We need to keep the recognition of that when we look at the tax burden.

Q238 **Siobhain McDonagh:** I would like to look at issues round the gig economy. According to published statistics, workers in the gig economy are younger than the general population and they lack employment rights. In these circumstances, is it right that they should be taxed differently than employees?

Professor Freedman: There is a great deal to be said about the gig economy and the protection of gig workers, many of whom I think are workers and will very soon be found by the courts to be workers, for employment law purposes, and therefore have certain rights. That does not fit into the current tax structure, where workers are not a group that is recognised for tax purposes. We have three different definitions, for



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employment law purposes, which are employee, self-employed and worker, and we have only two for tax. That is very confusing.

We need to look at the way we tax those people who are working, often for many different engagers, separately from the way in which we protect their rights. They should be paying tax and national insurance in the same way as if they were employees, because we should be looking for a level playing field across the board.

Q239 Siobhain McDonagh: Bill, in 2018 the OTS published a report on the gig economy taxation, yet it remains difficult to find clear HMRC guidance about the issue. What has HMRC done to implement the recommendations you made? What more should it do?

Bill Dodwell: That was a very preliminary report in 2018. We have done further work in that area, including a report published in October 2019 on reporting and paying tax. The role is primarily one for Ministers and Parliament. If we are going to end up changing the system, we need Parliament to enact legislation to do that. One point that the Office of Tax Simplification has covered in lots of inquires is that middle and lower-income people are very keen to manage their tax much better than currently. At the moment, if you are self-employed, your tax is paid twice a year, at the end of January and at the end of July. Additionally, it is delayed for quite some time. Once you start work, there is quite a long period before you start paying tax.

During our inquires, lots of people have told us that they would like to pay tax on a more regular basis so that they are on top of it and they do not have these gigantic, unexpected bills arriving at different times. The 2018 report you talked to referenced a system along those lines. There are opportunities to introduce more of that through the so-called single digital account, which is part of HMRC's 10-year tax administration strategy, and through that and elements of making tax digital to end up providing better information into the system and offering people the opportunity, but not necessarily the compulsion, to pay their tax monthly if they want to. I suspect you would find quite a lot of middle or lower-income people would wish to do that.

Q240 Siobhain McDonagh: That is why we get pay-as-you-go meters and credit on phones. If you do not earn much, you want it to be regular so you can afford it. Professor Freedman, you have probably touched on this, but to what extent is the gig economy a result of the tax differential between employed and self-employed, rather than a genuine improvement in relationship between employer and employee?

Professor Freedman: I do not think it is an improvement in the relationship at all. Tax has exacerbated the other incentives. As people have said, there are many incentives to not employ people, some of which are employment law incentives. That is exacerbated by the tax. If we look at certain platform providers, it is much cheaper for them at the moment to operate through gig workers than to take those people on. In



some cases we even see them offering to provide insurance and other things separately and privately, rather than paying the tax they could pay in order to provide those systems. They are clearly saving money from this. That is inherent in their argument that they would not be competitive if they were not able to use gig workers. That competitiveness is coming at a cost to those fairly vulnerable workers.

Q241 Siobhain McDonagh: Absolutely, Uber and Deliveroo might struggle to compete if they had to engage the workforce on the same terms as conventional employers.

Bill Dodwell: It is worth saying that almost all taxi drivers in the UK are self-employed. This is not something that is particular to a platform. If you look at the work from the Office for National Statistics, I think you will find that 90% of taxi drivers in the UK are self-employed.

Professor Freedman: I was being quite careful not to mention any particular platform.

Q242 Siobhain McDonagh: That was my fault. I find with my constituents that the rise of the gig economy makes more conventional employers attempt to reduce the terms and conditions of their current staff, in that they feel it is quite iniquitous, so it is a race to the bottom for a lot of the people I represent. Do we risk a two-tier workforce or a two-tier labour market?

Professor Freedman: We risk a very distorted labour market unless we sort out the rights of these people. That is a question for labour lawyers rather than tax lawyers, but I agree that it needs to be tackled.

Derek Cribb: I agree with Judith. I am going to sound like a scratched record, but this comes back to getting certainty about exactly what your employment status is, in the first instance, and then looking to see what the tax consequences are. I will not go into the economics of these large platform organisations, whether you call them employers or whatever, but the assumption that they cannot compete if somebody comes to be employed is for them to work out. There are some very smart people there. They may have to address their pricing or a number of issues, but to say they cannot compete is possibly a bit of a bold statement.

Professor Freedman: I was not saying that they could not compete. They could address their pricing and that is the answer. The market can deal with that rather than requiring tax to deal with it.

Q243 Siobhain McDonagh: Andrew, would employers welcome clarity? Do they want these workers taxed as self-employed or as employees?

Andrew Titchener: They would welcome clarity. We mentioned earlier the certainty piece for employers. That is very important. Judith mentioned that we have three different statuses for employment law and two for tax, each of which requires an independent determination. For every worker, you effectively need an employment, a tax lawyer and an



HR professional to decide their status, which adds a lot of cost to the engagement. In terms of the difference in statuses, for employers there is a lot more at play here than tax and things like that. In the end, you have to look at it in the round and say that some sectors are more predominately based on having employees, and others are more predominately based on self-employed and contracting relationships.

The CBI supports proper rights for workers and enforcement of those. We also need to think about the retention of that flexibility in the labour market, as much as we can, alongside those rights, to make sure that not only can employers engage with people in the way that is commercially right in their particular sector, but also many contractors like to engage in that way with their work. It is also preserving their ability to do that.

Q244 Siobhain McDonagh: Will further digitisation of business record-keeping help the Government to identify and tax those in the gig economy?

Bill Dodwell: There are a lot of different opportunities to be looked for through digitalisation. One is the provision of information by third parties, both to HMRC, the tax authority, and to the individual, naturally. I think that HMRC considers that digital record-keeping reduces careless errors, which is an important part of running a business. There is no doubt that slightly bigger businesses understand that having proper record-keeping and an accounting system helps them manage their business rather better, so there is an advantage of that. The mechanism for providing data to HMRC is yet to be determined, but the current plan seems to be that, from 2023 onwards, individuals in business should provide that data to HMRC on a quarterly basis.

The Office of Tax Simplification would like to see a much improved personal tax account and business tax account, in other words an online account for every citizen taxpayer in the UK, so that they can see and manage their tax affairs and correspondence with HMRC, make payments much more easily than currently and make claims for tax reliefs. All of that would support a much better approach and take real advantage of digitalisation. To implement that plan, HMRC will need not only to have the plan in the first place, but it will need money, because it requires capital investment up front to deliver all of this.

Q245 Felicity Buchan: Thank you for taking the time this morning. My questions are on the relationship between income tax and national insurance. Over the last 40 years, we have seen a big shift towards national insurance and away from income tax. Since 1980, basic rate income tax has moved from 30% to 20%, but total national insurance contributions by employers and employees have gone up 7.85% versus income tax declining by 10%. Andrew, do you think that shift makes sense? Why do you think we have embarked upon this shift?

Andrew Titchener: From an employer's perspective, as I said before, it is all about the total cost of employing somebody. To the extent that the shift is increasing that cost, you would expect that to have an impact on



total levels of employment and employment decisions going forward. I talked at the very beginning of this session about balance when you are thinking about tax. This would be an example of that. I must admit I do not have the answer, but it is worth looking at the balance to ask, "Is it right?" with the figures you have just given, particularly where cost to the employer is concerned.

Q246 Felicity Buchan: Judith, in your earlier remarks you slightly alluded to this, but it has implications. If you are a taxpayer who pays income tax but does not pay national insurance contributions, you are a beneficiary of this shift. I am thinking about people who have pension income, dividends or savings income. You alluded to this, but do you think this shift is wrong and how should we address it?

Professor Freedman: The shift has come about for political reasons, to avoid raising the headline rate of income tax, and it has not really been thought through. It has just happened for short-term reasons. It has definitely exacerbated the problems between the employed and the self-employed, as we have seen. A lot of the problems about employment status and IR35 would disappear if we evened it up. We would also catch forms of income that are being undertaxed at the moment and should be taxed. I would be very much in favour of restructuring around this if it were possible. I know there are big political problems, but I do not see any reason why we should not move gradually towards that.

Q247 Felicity Buchan: You say "restructuring". What does that mean? Are you proposing a merger of income tax and national insurance?

Professor Freedman: I am on record as having proposed a merger. Ideally, I would propose a merger, but one has to recognise the practicalities. That would be an immediate jump of the headline rate of income tax, which politicians would find hard to deal with. We may have to take steps towards that, but eventually that should be the aim. I do not feel that the current national insurance system is any longer what it was intended to be. It is not a contributory system any more. We could move towards merger, in my view, and remove a lot of the structural problems that we are talking about this morning.

Q248 Felicity Buchan: Apart from the political sensitivities, are there any tax issues in going to a merger, not in the actual implementation but in terms of unintended tax consequences?

Professor Freedman: The biggest problem is the employer's contribution, because that is a very large amount. I do not know how that would be distributed, but that would have to be thought about very carefully, along with whether you continue wanting to have an employer's or engager's levy. In itself, that reduces the incentive to employ and increases the incentive to use robots, AI and so on. That needs a really good look to see whether that is a sensible way to impose a levy on employers or engagers, or whether we should not be moving away from that idea altogether.



Q249 **Felicity Buchan:** Could you potentially be in favour of getting rid of the employer's or engager's contribution altogether and simply having it on the employee or self-employed side?

Professor Freedman: We would have to have something to replace it, because it brings in a lot of revenue. There might be an argument for moving away from any kind of employer's or engager's levy, which reduces the incentive to employ people, and to move to some other way, perhaps increased corporation tax or whatever, to collect that amount of revenue.

Andrew Titchener: I will pick up Judith's point about the employer's NIC. It raises a lot of money. We have some draft analysis in the CBI that suggests it was just over a third of the total tax contribution businesses paid last year, so it is a big levy. Could you move it to something like corporation tax? It comes back to the balance. What is the right balance? If you move that tax burden towards corporation tax, you are likely to have less effect on employment incentives but you might have more effect on investment incentives in other areas. The balance of that has to be looked at very carefully.

In terms of merging the two, from an employer's perspective it is really important to think about the practicalities and the fact that it would be welcomed where it is a genuine simplification. That is the really important thing. Although merging might appear to be simplifying things, it depends on precisely how it is done. Proper consultation and discussion up front is vital.

Q250 **Felicity Buchan:** Let me bring in Bill at that point. I think it is appropriate. If we were to look at a merger of these two taxes, it would clearly be a major change for the tax system. How should Government go about it and what challenges do you think we would face, in terms of implementation, if we made the decision to do that?

Chair: I think Derek might have wanted to quickly come in.

Derek Cribb: It was just a very brief comment. I have mentioned before that some of the downsides to self-employment are about red tape and complications. Many of those who go into business on their own accord are not experts at administration, et cetera. Broadly speaking, anything that simplifies the tax system for them is something we would welcome. There are reasons around pensions, state pensions, et cetera, but simplifying the tax system by merging employee's NI with income tax makes a lot of sense, and then perhaps looking further at the employer's side or the employment levy, whatever that might be, whether that is the employer's NI or some engagement levy for contractors. I can see benefits of there being a lever there that Government can pull as and when required, which the economy drives. Certainly, merging the employee side of NI is something we would go for.

Q251 **Felicity Buchan:** Derek, you have already alluded to having an



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engager's national insurance. How do you think that would work practically? Are there any downsides that you foresee?

Derek Cribb: I am sure there are greater minds than mine at the Treasury that could look at how that could be implemented. It could be part of the billing process and paid on by the contractor. Alternatively, there could be an additional taxation on that part of the P&L that is registered at the engager end. I would hate to be prescriptive in any way but I do not think it is insurmountable.

In terms of downsides, so far this is a higher-level concept. We have not worked through exactly how that would impact more widely. We are very happy to engage with people to work that through and see how we can make that function in a way that works best for everybody.

Bill Dodwell: Can I pick up that engager levy point? If you were to have an engager levy, it would only apply to part of the market. Think of a plumber. I would suggest that it does not look conceivable that, if any of us invited a plumber to come and fix something in our house, we would take off some tax and send it to HMRC. On the other hand, if you have a bigger plumbing firm that engages a lot of self-employed plumbers as part of that, it might have an engager levy. That is an illustration of the complexity around all that. It is not to say it is a bad thing, but it is a complicated thing to do. You would have to work out who was going to be liable for it.

The Office of Tax Simplification did some work in 2016, looking at merging the base for national insurance and income tax in relation to employment income only. That is important, because national insurance does not apply to pension income or investment income. Moving to extend it to that would mean a substantially higher burden for pensioners. There are about 12 million pensioners in the UK. About 6 million of them actually pay income tax, a little bit. It is a group that has benefited over the decades from the increase in national insurance, borne by them when they were employed, but not borne by them as pensioners.

Simply looking at merging the base for the two of them, the Office of Tax Simplification, working with HMRC's economics unit, estimated that there would be about 7 million winners and about 7 million losers from that merger. Examples of people who might lose are people with multiple part-time jobs. Currently, they pay less national insurance. If you merge the system to make national insurance cumulative and annual, like income tax and pay as you earn, you would end up putting up the bill that those people pay.

People who receive a bonus might end up paying more or less national insurance depending on where they fitted in the threshold. It is analysing all those differences that gave rise to that really significant number of winners and losers. The office also estimates it would take about five



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years to do. You would have to have a national insurance code and all that sort of thing.

The other really important and expensive part of the system to think about is that now we have a £12,500 personal allowance for income tax and a £9,500 allowance for national insurance. That £3,000 difference is a lot of money, to work out what is going to happen on that. You are talking about putting up tax after coronavirus. I suspect that giving tax away through that great chunk of money is not really on the agenda. We are going to have to think about how best to manage all that.

Those complexities are probably why no one has really looked to take that particular issue forward. If a Government were minded to do it, they would need to do quite a lot of smaller steps to accustom people to the new system. For example, if you say to the self-employed people Derek represents, "As of next year, your tax bill is automatically going up by 13.8%", the equivalent of employer's national insurance, that will be quite a big chunk for any group of people to absorb. You have to have a plan over quite some time for how you would introduce changes into the system.

Felicity Buchan: That is fascinating. I would love to continue, but I am being told that my time is up.

Chair: Thanks for that very insightful and interesting answer to that last question, Bill.

Q252 **Alison Thewliss:** I have some questions about limited companies and dividend taxation. Professor Freedman, the OBR has noted that there has been an increase in incorporations of businesses in recent years. Do you feel that this is motivated to any extent by tax?

Professor Freedman: The evidence is pretty clear that it has been, in part, tax motivated. There has been a lot of work with Datalab statistics and so on to suggest that there is a relationship. There is a clearly a correlation and the causation is to be guessed at, in part, but there is some evidence coming forward that it is tax motivated. You only need to go into the professional journals to see the advice that is being given to people, to see that they are being advised to incorporate for tax purposes.

Alison Thewliss: I wonder if any of the other witnesses feel that is the case as well.

Bill Dodwell: Work that the Office of Tax Simplification has done has demonstrated that there is a mixture of reasons here. It partly depends on the type of activity that the individual is engaged in. If you are a freelancer, up to now you have been positively encouraged by the tax system to set up a company to provide those services. As Derek said before, that brings extra administration with it. In other work we have done, we found that people do not understand it, and that is a big burden in this sort of thing. Nonetheless, there are tax savings.



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Work from the Institute for Fiscal Studies, using HMRC data, which is the Datalab that Professor Freedman mentioned, demonstrates that owners of companies, particularly smaller ones, can manage their tax, not unreasonably, to minimise the overall tax burden. For example, they do not take dividends if it would put them into higher-rate tax. They wait a year and take it when they might end up with a basic-rate tax burden. They have additional opportunities to save money in the system. The question that some of us would ask is whether that is a realistic way forward. Should we have that available to us?

Derek Cribb: There have been numerous reviews and papers produced on this over the years. I do not think any of them suggests that reduced tax is the primary reason for incorporation. The top reasons tend to come through fairly commonly throughout. Quite often, No. 1 on the list is protecting your personal assets, which is incredibly important for anybody setting up in a business. You do not want to put your house on the line every time. That is certainly a differentiator between being incorporated and not.

Business credibility is another significant issue. There are a number of organisations out there that will only engage people working through a limited company. These are the main drivers. I have not seen any report that has suggested tax benefit is the No. 1 reason for incorporation. Yes, it tends to be up there. It might be second, third or fourth, but protecting your assets, business credibility and access to contracts tend to be the leading reasons for that.

Bill Dodwell: The point on access to contracts is specifically because the current tax system relieves the engager of responsibility. That is why the engagers wish only to deal with a limited company, because it means the engagers have no responsibility for working out if this is a quasi-employee or not. That is part of the issue with IR35.

Professor Freedman: I agree with that totally. I have been researching this for many years. It is true that people usually put limited liability at the top of their list, but, when they are asked detailed questions about the limited liability they are getting, there are certain types of people who are not getting any limited liability at all from incorporation. That can be very illusory because most people will have to put their house on the line anyway to borrow any amounts of money. The extent to which you get limited liability protection, if you are just providing services, is very small.

Q253 **Alison Thewliss:** Mr Dodwell, the tax system tries to avoid double taxing dividends with income and corporation tax. This used to be done with a tax credit at the basic income rate. It is now done with an upfront lower rate of income tax on the dividends. Which system do you feel is the better system and is there a case for further change?

Bill Dodwell: That is a really difficult question. It is known in tax literature as the difference between the classical system, the one we have at the moment, and the imputation system, the one we used to



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have. The reason we have the system we currently have is because the imputation system, the one of giving you a tax credit, did not work at all for companies that invested overseas, paid tax overseas on their profits, then brought them back to the UK and tried to distribute them. That is why we eventually moved away from all that, and Gordon Brown was the initiator of that in 1998-99.

Given the international scale of things, we are probably better off with the so-called classical system, where, essentially, you have a lower rate to assume that tax is borne in the company. Often, it is, if you are dealing with a smaller UK domestic business, but there are occasions when it is not really borne in the company at all, which one needs to think about. Having that system imposes on you the need to look at other issues around how you tax a smaller company and its owner-managers. It is not as simple as relying on dividend tax, with or without a dividend allowance, as we currently have.

Q254 Alison Thewliss: In 2016, the OTS looked at a review into small company taxation and suggested a sole enterprise personal assets vehicle. Is that something you would still like to look at, or have things moved on somewhat?

Bill Dodwell: Things have moved on; that is the honest answer. Derek and Judith have made the point that, for some people, limited liability is perceived as a business need. It is a limited subset because often, if you want to borrow money from a bank, you have to secure your house or that sort of thing. In response to that perceived demand for limited liability but not needing the complexity of a company, the OTS looked at that. We have discovered that Government are not interested in taking that particular issue forward. Adding yet another thing into the mix probably brings its own complexities. No, we are not directly looking at that any further.

Q255 Alison Thewliss: I do not know if any of the other witnesses feel that there might be an alternative to limited companies and whether they have any proposals for that.

Derek Cribb: We have looked at the SEPAs. In the past, we have proposed something called the FLC, the freelancer limited company. These are both ideas as to how we can simplify the tax system for those who are self-employed but also potentially protect their assets, so looking at a particular, almost light-touch, form of incorporation that gives that level of protection and allows you to think about how surpluses might be distributed out of that entity in a much more simplified way.

If you only have one sole director, you can sit there and say, "Does it matter whether you are calling it PAYE or investment income and dividends?" The reality is that you have one source of money coming in and one source of money going out. Is there a way that we could have a much simpler approach to that? Whether it is SEPA, FLC or some hybrid or new version of that, I still think there is quite a lot of mileage in



looking at some sort of entity that gives those protections and allows simplification of the red tape as well.

Andrew Titchener: With the alternative vehicles point, I would make the point that, if you are going to bring something like that in, you still have the same problem of deciding who is allowed to set that kind of vehicle up. Who can benefit from that sort of vehicle? It is potentially more complex in terms of deciding who is in what vehicle and therefore what their status is. If you are going to do something like that, it needs to be very well considered and very clear as to who gets that status, so employers do not have to make another series of decisions as a result.

Professor Freedman: I cannot see how we are going to improve this situation, where we are trying to align treatment across different types of vehicle, by introducing another vehicle. That cannot possibly simplify things. It will create more boundaries. It will create more planning costs for the taxpayer, having to decide which of those vehicles to use. I would like to question the assumption that having a company is very complex. In the UK, it is pretty easy to set up a company and fairly cheap to run a company. Any vehicle that gave limited liability would have to have a certain amount of protections around it. Once you say that, you might as well set up a company, if that is what you want to do. Creating a new form seems to me to be definitely a complication, as I would say, rather than a simplification.

Bill Dodwell: I think that is ultimately why we agreed with that. It is very quick, simple and cheap to set up a UK company, but work the OTS has done has found that lots of people starting up in business do not understand the difference between a company and themselves. It is that sort of complexity that they struggle with, together with accounting. I know many will say that all self-employed people need to understand some accounting so they can work it out, which is obviously true, but I would suggest that there is an added burden when you put in an extra legal person, a company, as well.

Q256 **Alison Thewliss:** I will move to an area where there has been noted complexity, IR35. Andrew Titchener, the Government have clamped down on the use of personal company contractors in the public sector and they are extending those rules to the private sector. Can you tell me a bit more about the business view of this change and what you are looking for on that?

Andrew Titchener: It is fair to say that there is a lot of business concern about this change. We have talked already about the underlying uncertainties in the system. IR35 is just another layer on top of the problems with employment status. There is real concern about the fact that the changes coming up are moving the burden of enforcing the tax system from HMRC to employers. That seems to be somewhat difficult, as a challenge. We have some anecdotal evidence that it can be quite an emotional issue. I appreciate the change has been delayed, but some employers were already issuing determinations because they were



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starting to prepare for the original implementation date. We have had some anecdotal feedback that those conversations can be very difficult, where contractors do not agree with their determination for whatever reason.

I talked earlier about certainty and tax risk. I talked about flexibility as well, and that feeds into what I am about to say. We are starting to hear from employers now that, because of this change, and the change means that the tax risk is much more with the engager, the employer in my language, some employers are saying, "We will not engage with contractors any more". It is too risky, complex and expensive as a result of this shifting of the burden. Of course, it was risky and complex before, but now there is this added point that seems to have tipped things over the edge in some areas.

To me, that seems to be the worst of all worlds in many respects. It seems to have increased the complexity, difficulty and costs for employers and, at the same time, decreased the flexibility that the labour market has, because employers are reacting by saying, "We are not going to take advantage of that flexibility because it is too costly and risky for us at the end of the day". There are some real concerns there for sure.

Q257 Alison Thewliss: One of the things that I picked up on during the passage of the Finance Bill was that there had been a degree of a chilling effect on contractors being taken on, which seems to reflect what you were saying there. Have you any further evidence on whether that has been the case?

Andrew Titchener: It is a little too soon at the moment for us to have firm evidence. We are hearing it anecdotally. It is certainly something we will be gathering going forward. The changes come in next year and employers are starting to prepare for them now. We are likely to have much better evidence on the extent of that from next year.

Alison Thewliss: Derek, I imagine you would want to come in on this.

Derek Cribb: To be fair, I agree with pretty much everything Andrew has said. I would like to flag that we have seen 500,000 people falling out of self-employment in the last six to nine months. Those are ONS statistics. Normally, in a time of economic crisis, you would see more people going into self-employment. We are seeing absolutely the opposite and now we have a piece of legislation coming in, in the new year, when we want to encourage that flexible resource, which is disincentivising it. It seems slightly perverse to have IR35 coming in when you want to encourage people to be flexible and to help the UK economy out of a crisis.

Q258 Alison Thewliss: You mentioned earlier you felt the boundary on IR35 was really unclear. Would you agree with what the House of Lords has suggested in its recent report, that the IR35 scheme should be scrapped altogether?



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Derek Cribb: Yes, absolutely. I am a great fan of that report. It is a very thorough piece of work. I am surprised that it was not really listened to, particularly by Government.

Q259 **Alison Thewliss:** Do you feel there are particular reasons for that not being picked up further?

Derek Cribb: I could not hazard a guess.

Alison Thewliss: That is fair enough.

Q260 **Chair:** Possibly one of the reasons why the Government persist with it is to collect tax.

Bill Dodwell: There is quite a big amount of tax projected to come in.

Q261 **Alison Thewliss:** There was a question I was going to pick up with Bill Dodwell about how you would prevent tax avoidance within the current parameters of the system.

Bill Dodwell: As we have said before, we would encourage a longer-term or medium-term view of trying to narrow the differentials between the various taxes on labour income, national insurance and so on. If you did that, you would reduce the pressures generally. The other point—I gave evidence to the House of Lords on this one—was that we favour a new and different statutory test of employment, so people have a much clearer understanding of where they sit on the boundary.

We are not saying you should enact a piece of statute to encompass the current, very muddled case law system, which leads to disputes. People have said that HMRC wins cases and loses cases, which is absolutely true. You can see all that. We just need a better system. I would suggest we ask, in today's modern environment, who should realistically be treated as self-employed and who should not. Professor Freedman has made the point that that is different from employment taxes. Yes, of course, because there are three statuses under employment law. Equally, clarity is needed there. You do not benefit from having cases go all the way to the Supreme Court as to whether somebody is or is not a worker. That does not help the system

Q262 **Alison Thewliss:** What would be the key tests for you?

Bill Dodwell: You should ask, "What would the tests be?" There might be some professions or trades, whatever, where you say, "This sort of thing is fundamentally a thing of self-employment". You might ask yourself, "Does the individual spend three-quarters of their working time working for a particular engager?" There are a range of different options that you would realistically look at. When we brought in a statutory test for tax residence for individuals, we spent three years doing that, asking the questions of how we should approach that. We should do exactly the same sort of thing in this area too.



Professor Freedman: I absolutely agree with what people are saying about IR35 and the off-payroll system. One of the problems is that IR35 was based on the case law and that was the mistake in the original design. There was no reason why we could not have come up with a solution that was not based on the case law. As people have said, the case law is muddled. The case law is nuanced and complex for a reason, and that is because it is very fact-based. Different facts give rise to very different decisions.

The idea that we can come up with a simple difference between the employed and self-employed that everyone will agree and that will work for every purpose sounds wonderful. It sounds as if it would simplify things. Either you would have a very rigid test that looked at how long people had worked for a certain engager or not, which would be very easy to manipulate and play around with, or you would end up with a nuanced test that would end up having as much baggage as the case law. That would be your problem. The simpler the test, the easier it is to engage in creative compliance and to play the system. That is why for administrative purposes you might need one test and for other legal purposes you might need another test. We are not all going to agree on one simple test.

Taylor recommended control as a test. That would be a disastrous test, because control is not a very good way of distinguishing between whether someone is an employee or self-employed. A brain surgeon can be an employee and yet he is not controlled in the sense that some of the case law talks about. There is not a simple test or simple difference between the employed and self-employed. Just by saying we want there to be, it does not mean we can create one.

Bill Dodwell: The statutory residence test has a lot of nuances and different point counting, but you end up with a bright line. In today's digital world, you need to end up with bright lines and accept the consequences of that. If the tax was not so different, you would not be wound up so much about whether somebody was self-employed or employed.

Professor Freedman: I agree on that.

Q263 **Rushanara Ali:** Good morning. I wanted to pick up on a couple of things that were raised earlier, before I go on to tax administration and digitisation. Picking up on Siobhan's question for Bill Dodwell, you talked about the self-employed, cabbies in relation to Uber, for instance. There is a big difference between a company like Uber, worth £50 billion to £70 billion, and the local cabbie down the road in a constituency. Can we address some of these inequities in the way that big companies play the system and are not true to the essence of what they are about? Is there more we can do on that? You were quite determined in your point about the cabbies being self-employed, but Uber is not any ordinary cabbie.



Bill Dodwell: It is not right for me to comment specifically on one particular player in the market. If you read our reporting and paying tax report dated October 2019, released on Halloween, you will be pleased to know, we essentially said that there was a real case for information provision and even possibly considering withholding in a market where there are a whole range of engagers and, typically, the individuals providing the services do so through the means of an engager. It is exactly the same dealing with a global company on a platform, a very large private hire firm primarily based in the UK or Ealing taxicabs. When I want a taxi, I phone up a taxi firm. I do not phone up a particular driver. You should look at that market situation and whether there are intermediaries or third parties there.

Holiday properties are another case. Again, almost all that market is dominated by a whole range of intermediaries, not just one of which we can all think. There are plenty of others there. You should ask those intermediaries to provide information to HMRC. We think overall that will be a help to taxpayers generally. That was the basis of our work in that report there.

Q264 **Rushanara Ali:** There is definitely work that needs to be done. In the age of technology and innovation, nobody is denying that these companies have provided an innovative solution and it is not all bad, but there are areas that create a lot of concern, particularly around rights and so on. I suppose I am adding to the complexity in raising the question about what we do in relation to intermediaries.

Professor Freedman: What Bill is suggesting is precisely what I was talking about. We have a particular problem with platforms. We tackle that problem with a set of definitions that work for that area and deal with it, both from a rights point of view and from a tax point of view, by looking at that particular set of problems.

Bill Dodwell: It is important that you do not distort a market by putting up a huge barrier for one of the players in the market, such that you end up with a migration to other players in the market generally. That would be a really important consequence to consider in designing a system for the future.

Q265 **Rushanara Ali:** Thank you. That is really helpful. Moving on to the digitisation agenda, you have talked about the benefits. Can you point to any issues that are coming up, particularly for those who are self-employed, where the downsides might be and how Government could address those ahead of the implementation that comes into place by 2023?

Bill Dodwell: The Government have mandated Making Tax Digital for VAT. That, essentially, requires a business that is required to be VAT registered to maintain digital records and submit those digitally, rather than typing them in, to the HMRC portal to submit their VAT return. That is a system that, by and large, has gone pretty well. There are about 400



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different software providers, mainly because there are lots of different industries, specialties and that sort of thing. That is why there are so many different software packages out there. Over 400 have adapted to be able to provide the VAT information into HMRC.

The challenge when you move to income tax is that you are moving smaller, in that you are going to a population that is not VAT registered, so you are imposing requirements on them for the first time. We would suggest that it would be as well to start proving a system at the top end, with people already using digital systems, and then move on to people who are introducing those digital accounting systems for the first time, so start larger, if you like.

You would also need a system of, essentially, combining information. For example, if you have a self-employed person who owns a buy-to-let property and has some dividends or interest income, you need something that is going to take all those different sources. The business accounting package the person will use for their self-employed business may not be the same as for buy-to-let accounting and will not necessarily pick up interest, dividends or anything else. You need something in that sort of area and inviting the market to deal with all that is definitely worthwhile.

There is also possibly the case for looking at a cash incentive. Back in the time of Lord Carter, who was one of the pioneers who looked very extensively at digitising tax, he recommended, and it was introduced, incentives for businesses to submit data digitally, in the form of real money off. It gave a bit of incentive anyway, sent a really good signal and was not massively expensive, but it was a contribution to the substantial costs businesses take when they have to buy a new accounting package and all that.

Most of this is focused on microbusinesses, single individuals or a small number of people working together. It also important that HMRC thinks harder about larger businesses, for which this is probably a completely unnecessary form of information gathering. Large businesses already provide very substantial information to HMRC and probably do not need to add to it.

Q266 Rushanara Ali: How realistic are the digitisation plans, given delays that have occurred in the past?

Bill Dodwell: At the moment, we have a sort of three years' time announcement, which ought to be sufficient time to allow the market to develop. As I say, if we started with only part of the market, for us that would be a good thing, because it would help prove the robustness of the systems before extending them down to those for whom a much bigger change might be anticipated.

Q267 Rushanara Ali: Despite the current crisis and upheaval, you do not see a major issue in terms of meeting the target, provided that the approach you are suggesting is taken.



Bill Dodwell: I think so. It is a bit hard to know whether HMRC will be able to adapt its systems in time, given all the other burdens it has of trying to work from home, Brexit, the new information systems needed for that and everything else. We have emphasised it is really important that the single digital account, that interaction between the taxpayer and the tax authority, is part of this, so that there is a benefit all round, rather than data arriving in an unstructured manner and not necessarily being very useful to HMRC.

Derek Cribb: I have a couple of points there. I have talked previously about the extra burden that comes with being self-employed. As we go into digital taxation and that being rolled out to the self-employed over the next three years, I am keen that that is kept in mind. There was a conversation earlier about perhaps collecting data on a monthly basis. Let us not try to make that mandatory. If people want to have the facility, yes, make the facility available, but do not compel people to report that often. They are trying to earn a living.

It is important to remember that average self-employed earnings are lower than average employee earnings. In many cases, these are not high-earning, sophisticated people and we are asking them to go digital. Let us try to keep it as simple as possible for them, with quarterly rather than monthly submissions of data. This will be yet another financial burden in many cases, because they will now have to move off paper records or Excel spreadsheets into integrated digital technology and there is going to be another cost associated with it. These are all additional burdens that you see on the self-employed that you would not see on somebody in a similar role perhaps who was in full-time employment.

Q268 **Rushanara Ali:** Some would argue that they have been shafted during this crisis, particularly those who have been identified as being excluded without any support from the Government, as you rightly pointed out earlier. Can I bring in Andrew and others on one final question? Does digitisation help tackle tax avoidance? Will it, by a substantial amount?

Andrew Titchener: That is impossible to say. The aim of digitisation is absolutely laudable in many respects, in the sense of giving HMRC more up-to-date information on a more regular basis. That has to help the administration of tax, you would think, if it is done well. The really important thing is that the phasing and consultation of the process is done with a view to the fact that there are going to be a lot of hurdles to get over for many businesses to implement this properly. The only way it is going to work effectively for HMRC is if businesses have time to implement it properly and adjust to the new way of working.

If we are talking about tax and the right amount of tax, there is discussion in some of the documents that have come out with Making Tax Digital of whatever stripe that this is going to be a simplification and will make everything easier to get right, but it depends on how you do it. If you digitise the existing tax system, you are going to digitise all the complexity that exists within in. If you want tax to be easier, easier to



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get right and all that, digitisation is one step but looking at the tax system again and the complexities in there is also very important, if not more important than digitising it.

Q269 **Rushanara Ali:** Professor Freedman, did you want to come in on the point about tax avoidance, whether digitisation will help?

Professor Freedman: I was going to agree with Andrew. When you are looking at digitisation, you have to look at the underlying system. You are not going to deal with avoidance without dealing with the underlying system and the complexities in the system that give rise to avoidance, particularly having lots of boundaries, which is what mostly gives rise to avoidance. The two have to go hand in hand.

Going back to your point about the people who have been excluded from support, had we had more information in a better form available to HMRC, it might have been possible to exclude fewer people. One of the barriers to providing them with support was not having sufficient information in the right form. In the end, this should be a way of getting more information for the benefit of taxpayers, as well as reducing avoidance.

Q270 **Harriett Baldwin:** I have the pleasure of coming last, which means we have covered quite a lot of the topics already. Each of the experts, if you had to choose between simply implementing the results of the Taylor review, setting up a tax commission, setting up an independent review of off-payroll working or A N Other suggestion, what would be the one thing you think the Government should do?

Professor Freedman: I do not think we need any more reviews. We have had plenty of discussion. We need the Government to have the will to do something about this and to have the space and time. I understand why it has been very difficult for officials, and particularly now. They have had so many preoccupations. We need to take some of the information and analysis that they already have from the IFS, from the Resolution Foundation, from Taylor, and sit down with it, work out the best way forward and not think about this short term but slightly longer term.

Q271 **Harriett Baldwin:** What would you actually do?

Professor Freedman: I have written what I would do in many places. We set out in Mirrlees what we would do. I would merge tax and national insurance. If I cannot do that immediately, I would take steps towards doing that more gently. I would have a roadmap so that everyone knew which direction we were going in. I would get rid of IR35. I would not need it any longer because there would not be the vast distinctions.

Q272 **Harriett Baldwin:** Bill, what is the one thing you would do from here?

Bill Dodwell: I would have the medium-term plan of looking at the overall burden of tax between employment, self-employment and those



who provide services via companies. It will lead to a whole range of solutions and things to look at, but I would start off down that path and spend some time looking at how it would all work through. Alongside that, I would increase digitisation at HMRC.

Derek Cribb: There was a quote from Paul Johnson when the Mirrlees report was issued: "There is little about the UK tax system that looks like it was deliberately designed". That is very perceptive and as true now as it was then, whether it needs a wholesale review or some people to get together in a room and look at all the reviews there have been, but actually design a tax system that is fit for purpose. I would be a great believer in going back to first principles. What are you trying to achieve? In the judgment of the experts, what is the right balance of personal versus corporate taxation? I would start from there. It is a longer-term way of doing it, but trying to get something that is fit for purpose and plays into the digital world in which we are all existing and which will continue to become deeper and deeper.

Q273 **Harriett Baldwin:** Andrew, from an employer perspective, what administrative problems do you get from NICs, not the cost of NICs but the administrative problems as well? Elaborate on the one thing you would choose to change if you could.

Andrew Titchener: As the CBI, we are very clear that any change to the employment status for tax should follow alongside the Taylor review. The two should be done together. Longer term, I agree with Professor Freedman that setting out where you are going with it, and giving that proper consultation, is vital.

NICs have been around for a long time, so they are embedded pretty well into business systems. I would not necessarily suggest that, at the moment, systematically, from an administration perspective, they give a huge amount of problem. The problem arises from knowing when you need to withhold NICs or not because of the status problems. If you fix the status uncertainty issues, you help to reduce those issues with NICs.

Q274 **Harriett Baldwin:** Bill, earlier you touched on the recommendations that the Office of Tax Simplification has made, particularly on NICS, and what the barriers have been to implementing that. Can I ask you to do a wrap-up point on all this, in terms of what you are prioritising that you would like to see at the Office of Tax Simplification? What is left to do, specifically on NICs? Could you also add in some points about whether NICs should continue into pension age? I know this has also been discussed as a potential simplification.

Bill Dodwell: Let me take that last point. Yes, there is a real case that, if you are employed or self-employed past pension age, you should pay national insurance just the same as if you are under pension age. That is not a cost-free option from the Exchequer point of view, because some people would end up accruing additional years' benefit towards their pension. Nonetheless, for us it looks like entirely the right thing to do.



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Overall, it would raise money and would also allow some people to qualify for a better pension through all that. That is a relatively small thing to do, but I would definitely lurch off in that direction and take some money out of the system in that sort of way.

I agree completely with everyone who has said that you need to look at some aspects of the system before you digitise. That is definitely true at the smaller scale, so trying to have a simplified form of corporation tax in a manner that works more straightforwardly, as opposed to theoretically imposing big company rules on miniscule companies. That would be a good thing to do before we consider any form of Making Tax Digital for corporation tax.

I welcome the 10-year tax administration strategy from HMRC. It essentially says, "We, HMRC, have to digitise. You, business and personal taxpayers, have to engage with us more digitally, but you will get a lot of benefits out of doing that". That is a really important pathway to set down. Looking at additional third-party information to be provided into the system is a really important way of helping regular people comply. There is no doubt bigger organisations have more resources and are more capable of taking off tax, providing reporting or both. Asking them to do a little more so as to benefit millions is definitely a whole area worth looking at more generally.

On the employed, self-employed or company question, the so-called three-person question, as I gather it is now called, the Office for Budget Responsibility is talking about differences worth £5 billion plus a year to the UK economy. That is why it is a question that has to be picked up. If we move to a world with a greater level of self-employed people or people with a mix of employment and self-employment, we have to have a tax system that deals with all that.

All this has to take account of the UK's international position. Exchange of information is really important for tax authorities. We in the UK need to work extensively with the OECD and others to provide that exchange of information. As it becomes possible to provide those services from outside the UK into the UK, we need the information to understand what is going on, to decide whether it is taxable and so on, but so do lots of other countries. There is quite a lot to look forward to, all driving off that digital agenda that we see taking part of the economy.

Chair: Treasury Questions are about to start and a number of us have to contribute, so I wanted to wrap up very briefly. Thank you so much to all four of our panellists. We have asked some very important questions about the different tax statuses of the self-employed, the employed and those who work in companies. We did not achieve unanimity as to whether the tax differences were justified, but we certainly heard both sides of the argument put very clearly. Thank you for that.

We agreed that serious distortions flow from this, both in the labour market and in, for example, the growth of people incorporating and



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working through small businesses, leading us all, unfortunately, to the dreaded IR35. I think we are all agreed that this is best abolished as soon as possible. It may be a case of doing it in a way that perhaps means it is redundant altogether because of tax changes, rather than just dispensing with it and the Treasury taking a rather large tax hit as a consequence.

The Chancellor, when he brought in SEISS, made reference to possible changes to the tax arrangements for the self-employed. That may suggest that he is looking at that space quite carefully. I think our discussions today will be particularly pertinent as to what may or may not occur going forward. Can I finish once again by thanking you all so much for contributing? That has been extremely helpful to the Committee.