

Treasury Committee

Oral evidence: Tax Reliefs, HC 723

Wednesday 1 March 2023

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Members present: Harriett Baldwin (Chair); Rushanara Ali; Anthony Browne; Dame Angela Eagle; Emma Hardy; Andrea Leadsom; Siobhain McDonagh; Anne Marie Morris.

Questions 94 - 187

Witnesses

I: Kathryn Cearn, Chair, Office of Tax Simplification; Bill Dodwell, Tax Director, Office of Tax Simplification.

Examination of witnesses

Witnesses: Kathryn Cearn and Bill Dodwell.

Q94 **Chair:** Welcome to the Treasury Committee evidence session on tax reliefs. I am very grateful to our witnesses today for coming in to talk to us. Can I invite you both to introduce yourselves for the benefit of the Committee?

Bill Dodwell: Hello. I am Bill Dodwell. I am the tax director at the Office of Tax Simplification. I additionally have a couple of other roles. I sit on HMRC's General Anti-Abuse Rule Advisory Panel, and I am also the technical editor of a tax magazine.

Kathryn Cearn: I am Kathryn Cearn. I am the chair of the Office of Tax Simplification, and I have various other public sector non-executive roles.

Q95 **Chair:** Thank you very much for being with us this afternoon. The Committee is very interested in exploring the decision that Kwasi Kwarteng took as Chancellor to abolish the Office of Tax Simplification and fold it into the work of the Treasury. You may well want to contest the words I use there, but we have an afternoon to take evidence on that.

I am old enough to remember when George Osborne set up the Office of Tax Simplification. The argument at the time was that this country had a tax code of 11,000 pages, that the tax code had mushroomed over the last decade, that it had become far too complicated and that there was



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important work to do on simplification. I will start with a simple statistic. There were 11,000 pages back in 2010. How many are there now?

Bill Dodwell: I cannot answer that one. If I am fair, that is not the best way to assess complexity. The OTS did a study and it counted all the relevant pages. It came up with, at the time, about 6,000 active pages, albeit they were published in a series of books that totalled about 15,000.

The reason was they included a lot of repetition. You could just take out one book, and it had the administrative procedures copied from several other places. The other reason was that those pages included previous years' law; it was not just the law that was relevant to the point today. I do not think that is what matters.

Q96 **Chair:** Can I ask simply whether the tax code is longer and more complicated than it was in 2010?

Bill Dodwell: It is longer. The principal reason is because new taxes have been introduced by the Governments we have had since 2010. The Chartered Institute of Taxation calculated that in the last 20 years we have had, on average, one new tax every year.

Q97 **Chair:** Is the Office of Tax Simplification being closed down because you have been so successful at simplifying the tax code?

Kathryn Cearn: You would probably have to ask the Government for their direct reason around that. When we have looked at how effective we are, it has not necessarily been about whether the tax code itself has been simplified. As Bill has mentioned, we do not necessarily look at that as the primary measure of simplification, although access to legislation and the guidance related to legislation is very important.

We have predominantly focused on the interrelationship between taxpayers and the revenue authorities, how simple their engagement is and how easy it is for people to deal with the tax system, particularly focused on sole taxpayers, those who cannot afford representation and smaller businesses. That is predominantly where the focus has been.

Some of the things that have developed over the last few years in terms of the digital agenda have been very focused on that. To the extent that there is a digital interface, there is the ability to make things much more straightforward for those who are digitally enabled and to allow them to interact with their tax affairs in a more straightforward way.

We have tended to look at a wider range of issues than simply what the legislation says. We have looked at the administrative side of things, at how people interact with HMRC and where they fall down. Where they have problems, we focus on why that problem is being created and whether there is an ability to simplify.

Q98 **Chair:** Can you give me a few examples of where you have successfully simplified the tax code during the decade-plus you have been in existence?



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Kathryn Cearn: Bill might want to give you an example. I should be very clear here: we do not simplify the tax system ourselves. We advise as to what we think would be good ways to simplify the tax system.

Q99 **Chair:** Can you point to some examples of where you have advised a simplification that has been successfully implemented?

Bill Dodwell: Yes, of course. I would highlight the cash basis, which is a simpler way for freelancers, those providing mainly labour-based services, to record their income and expense. They record the money they get and the money they spend. They do not need to do longer and arguably more informative accounts. That was recommended by the office and has been a huge success. Some 1.2 million people currently use that to report to HMRC.

Q100 **Chair:** Can you think of any other major successes over the last few years?

Bill Dodwell: Yes, our work on guidance. HMRC's guidance is really important because 99.9% of people do not read the law, and nor should they. The guidance is critical. Our report recommended the introduction of the specialist team and a head of that team. That has happened. It recommended an external panel involving a wide range of taxpayers, academics, advisers and so on. That has happened. HMRC has taken on a whole range of other initiatives.

Q101 **Chair:** There must be a lot of things that you are frustrated you have not been able to simplify. I am sure I am speaking for other members of the Committee, but, when we meet with businesses in our local constituencies, they all still make the point that it is very complicated. What do you feel most frustrated by, as you end your autonomous existence as an office?

Bill Dodwell: Going back to what Kathryn said, our job is to advise and it is not to do. You can look and see the reports that have not really been taken up. We have been asked by Chancellors to do reports on inheritance tax and capital gains tax. A small number of the measures were taken up. The administration of inheritance tax is being simplified, which is excellent. On capital gains tax, if you sell a residential property with a gain, you used to have to report after 30 days. Following our report, it is 60 days, which is a useful thing.

Where people—married people or civil partners—separate, they had to pass their assets between themselves within the year of separation. There is now a much longer period of at least three years and potentially longer. There is a range of stuff, but it is smaller things.

Q102 **Chair:** Do you feel that taxes are simpler? Apart from the fact that a lot of new taxes have come in, do you feel that taxes are simpler than when the Office of Tax Simplification was set up?

Bill Dodwell: If you take the overall tax system, no, it is not simpler. The areas the office has worked on have been improved, yes.



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Q103 **Chair:** In terms of the way you work, can you think of any things that, in retrospect, you wish you had done to prevent a Chancellor taking the decision to dissolve your organisation as a separate office?

Bill Dodwell: I still do not know why Kwasi Kwarteng made that announcement. It contained no reason for why the office should be closed. The Government and future Governments will miss some of the attributes of the office.

Q104 **Chair:** You regret the decision.

Bill Dodwell: Yes, I do.

Kathryn Cearn: Yes.

Q105 **Chair:** You regret the fact that Jeremy Hunt has not reversed it.

Bill Dodwell: Yes. The Government will lose a champion for simplification. When the office was created, Sir Edward Troup, the former head of HMRC, said that people were sceptical about it, but it built a reputation. The result was that officials then spent a lot more time thinking about simplification. They will miss that champion role; they will miss having a dedicated team that can look in depth at a range of issues; and they will miss the candid and frank comments you get externally that will not go to HMRC.

Q106 **Chair:** Kathryn, as chair, can you think of things the office could have done differently that might have made you more powerful, more effective and got more MPs fighting to stop you being shut down?

Kathryn Cearn: That is a difficult question. The whole focus was on the quality of the output in terms of the data it was based on and the reasoning behind it and an acknowledgement that there were trade-offs that always had to be made. Simplification is not an end in itself; it should be part of the overall process.

What I regret most is not what we could have done. We are not a lobbying organisation or anything like that. We vouch for simplification, making things easier for taxpayers and simplifying things for the revenue authorities as well.

If I think about what we might have done going forward, there are some areas we could have looked at and advised on in more detail. We could have done more of the cross-cutting work we did on things like the digitalisation of the tax system and how that interfaces with taxpayers and businesses. Hopefully, we would have helped to make that a better system so that people found it easier to do the right thing, found that their tax information became more accessible and found better ways of doing things. We might well have started looking at the more structural aspects of how that worked in practice.

Q107 **Chair:** I am just putting this out there, but you probably could have done more to publicise your work with events in Parliament. I do not know whether any of us were ever aware that any of these things happened.



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I want to get on to an important topic, which is this OECD minimum tax rate of 15%. It was an international agreement of all OECD countries, but our Committee understands that the US has not yet been able to implement it, the EU is urging member states to implement it but none of them yet have, and yet the UK is planning to bring it in, I believe, in this year's Finance Bill. Are there any first-mover advantages in being the first to implement a minimum 15% tax rate?

Bill Dodwell: You are talking about pillar 2. I do not think that the UK is going to be the first to implement.

Q108 **Chair:** That was not my question. My question was about whether there are any first-mover advantages. There are no first-mover advantages; this is something that has to be done at the same time, does it not?

Bill Dodwell: It is better done with other people. When it came to the base erosion and profit-shifting work, which was the stuff that preceded this, the UK was indeed one of the first to go with it. It did get some extra money from all of that. When I worked at Deloitte, I thought that taking those measures was worth another 5% on corporation tax.

Q109 **Chair:** Which other countries might bring it in at the same time?

Bill Dodwell: The EU will go at the same time. They have a directive. They have agreed that directive. Member states will be obliged to adopt it and put it into law.

Q110 **Chair:** What about the US?

Bill Dodwell: The US almost certainly will not.

Chair: So they will not adopt it? They were very much behind it.

Bill Dodwell: They have different provisions, as you have probably heard from others. The US has its own tax system. It also finds it immensely difficult to change its tax system. There are only a really rare number of occasions when US federal taxation has been changed. It is unlike the UK.

Q111 **Chair:** You cannot see the US ever changing it.

Bill Dodwell: No, I cannot.

Q112 **Chair:** That is very interesting evidence. In closing, I wanted to clarify something. I understand that you were set up in statute, so it will require a vote in Parliament to shut you down.

Bill Dodwell: Yes.

Q113 **Chair:** Your expectation is that that vote will be in the Budget.

Kathryn Cearn: Yes.

Bill Dodwell: It will be in the Finance Bill after the Budget.

Chair: That is what you have been told will happen.



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Kathryn Cearn: Yes.

Bill Dodwell: If you wish to vote against that proposal, we would be very pleased.

Q114 **Chair:** You would welcome us voting against it.

Bill Dodwell: Yes. The Government and indeed the country would be better off if it retains us than if it abolishes us. We are not an expensive body, and we have done good work.

Chair: It is so lovely when we get clear evidence.

Q115 **Andrea Leadsom:** To follow on from that, I would certainly support not abolishing the Office of Tax Simplification, just to be very clear right back at you. However, I would just like to follow up a bit on the point of the OTS. I was on this Committee when the OTS was established back in 2010 and I was a big fan of it. I was also involved in an effort by Conservatives then in Opposition to do a great big tax review. I was very optimistic about it, yet we have not really seen much from you.

My question, having set out the fact that I think the OTS is an important thing, is: what more could you do? You declared that there were 1,042 tax reliefs in operation, for example, and you decided against your commission from the Government to review all of them, and to look at only 155 of them.

I do not need you to opine on that, but why is it that, over the last nearly 13 years, you have not focused on major eye-catching things that would really transform tax simplification? That is what the country was calling for. I distinctly remember that back in 2010 we wanted to see that. We were all very much aware that, with the financial crisis and the disaster businesses were under, they needed to see a much easier regime. Why has the OTS not been able to deliver that?

Bill Dodwell: The question really is, why have Chancellors not been able to deliver that?

Q116 **Andrea Leadsom:** You can choose the question, but why has it not happened?

Bill Dodwell: Let us take one of our flagship reports, which was about income tax and national insurance. As you know, an employed person pays both income tax and national insurance. There was substantial work done on the alignment of those. That essentially meant charging them on the same base and making national insurance a cumulative tax like income tax, which is cumulative.

The report that came out highlighted that about 40% of the workforce would be affected by those changes. There would be something like 6 million or 7 million winners and 6 million or 7 million losers. In light of that, the then Chancellor, Philip Hammond, decided not to take that piece of work further.



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It would have been a simplification, but it would not have been simple to deliver. It would have taken five years, the office of the day estimated, to get from where we were to that future thing, but it would have made life easier.

Q117 **Andrea Leadsom:** That is really clear. Is it your view that the reason Chancellors do not take up your recommendations is because they are administratively difficult to achieve or because they are politically difficult to achieve? What is your opinion?

Bill Dodwell: There are two reasons. Politics is one. You have evidence before you from the Institute for Government and others. Winners are happy and do not tell you; losers complain and tell you very loudly, obviously. That is an important thing.

Another aspect is the capacity of the system to make changes, which includes HMRC's technology, which is not as up to date as we as a country would wish it was. We should be thinking about our whole capacity to draft law, which the Office of the Parliamentary Counsel has to do, and the space in the Finance Bill to make all those changes. There is no capacity for lots and lots of changes, even if the net result after that transition would be a simpler system.

Q118 **Andrea Leadsom:** Yes, even if it would be better. It is interesting to look back at 2010 when we created the FCA, PRA and so on, which were all independent regulators. The OTS is just an advisory body. In hindsight, would it have been better if the OTS had been a regulatory body that could require simplifications to be made rather than just ask nicely?

Bill Dodwell: No, in my view. The judgment of what taxes to levy and how to levy them should rest with Parliament—with you.

Q119 **Andrea Leadsom:** Yes, absolutely, in terms of amounts, but what about in terms of simplification?

Bill Dodwell: You cannot divorce amount from technicality; the two are combined.

Q120 **Andrea Leadsom:** That is easily said, but—forgive me—the Bank of England could say that about monetary policy. It could say, “We do not want to lower interest rates because savers will be upset”. That problem was solved by the Labour Government with the independent Monetary Policy Committee. It took that out of the hands of politicians so that politicians would never again be accused of creating winners and losers. Is that not the same with the Office of Tax Simplification?

Bill Dodwell: It would not work as well as that, no. The two are really aligned. It is for the Government to take responsibility for their tax decisions.

Q121 **Andrea Leadsom:** Yes, in terms of amounts, but in terms of simplification, we are now at the point of a ridiculous volume of tax rules, are we not?



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Bill Dodwell: You cannot just ditch some bodies of rules and just rely on rates. Your inquiry is about tax reliefs. One of the things Governments routinely do is add additional reliefs into the system; very rarely do they remove them from the system. They add them because they seek an economic objective—to promote more activity or whatever.

Something like R&D tax credits are designed to promote more R&D in the UK. Film tax relief is designed to get more films made in the UK. The UK wants all of the economic activity that goes with both those things. That is a decision for the Chancellor.

Kathryn Cearn: I would just add that we have pointed out in reports where we think specific reliefs or elements of the tax code are not necessarily achieving their original policy objectives. Again, there has tended to be a structural impediment. When we have gone back and looked at whether things have done what they were originally designed to do, it is usually due to a poor initial design or because, behaviourally, they have not had the impact that was expected.

One of the useful things the OTS has done, outside the glare of the Budget light, is go back and look at these things and say, "Are they achieving what they were designed to achieve?" By definition, if they are not, they are a complexity.

Q122 **Andrea Leadsom:** They are an unnecessary complexity. They are potentially passed their sell-by date; they are no longer needed.

Kathryn Cearn: Yes, absolutely.

Q123 **Andrea Leadsom:** That is this tidying-up role. To come specifically to this issue of 1,042 tax reliefs, I remember a previous Committee where nobody could number how many tax reliefs there were—no one had a clue. You figured out there were 1,042, but you looked at 155 of them. Why did you look at only 155?

Bill Dodwell: The mandate given to the office at that time by George Osborne was to identify reliefs that were not needed in the system with a view to reducing the clutter. That is why a relatively small number were looked at. You could manifestly see that lots of reliefs were needed in the system. That is why it looked at a smaller number and recommended a smaller number still for abolition.

Kathryn Cearn: One of the positive things that came out of that work, though, was that more work was then done by HMRC and the Treasury to monitor reliefs and at least to keep a list of them in front of it. They were doing more of that. Before that, people were not going back and looking at the reliefs; they did not even have a complete list available. That is not happening now. They are much better at keeping an eye on what reliefs are there.

Q124 **Andrea Leadsom:** That is really interesting. Thank you, Kathryn. Would you say, therefore, that the outstanding reliefs that are pointless are gone? Is there still more tidying up to be done?



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Kathryn Cearnys: You cannot ever say that because conditions change as well. The things they were originally produced for perhaps go away, or the economic driver the Government were trying to encourage may have disappeared or they may have become self-supporting so they do not necessarily require that kind of encouragement anymore. Things can just change over time around that.

I would not necessarily say any of them are not redundant. They could well be. It is one of those things where you would have to keep it constantly under review to see not only whether they are working and whether they are still required, but whether they need to be replaced by something better because things have moved on.

Q125 **Andrea Leadsom:** For a time in 2010, the Government had a one-in, two-out policy on regulation. Would that be something that would be valuable for any future Office of Tax Simplification?

Bill Dodwell: No, it would not. You cannot ditch two reliefs in order to introduce a new one. No, that would not work. There is a whole range of stuff that should be looked at. When we have done subsequent reports, we have looked at reliefs in certain areas.

For inheritance tax, there is a small gifts relief of £250 and an annual £3,000 exemption for gifts. Those limits were set about 15 years ago and they are way too small to be useful for anybody. The point was to save people the administration of keeping records, but it is obvious that they need to be uplifted, if that was the purpose.

Kathryn Cearnys: Yes, and possibly consolidated in a way that makes a bit more sense for people so it is easier for their record-keeping as well as being in line with current asset values and what people feel they can give.

Q126 **Andrea Leadsom:** That is a really good example of something that has not been changed in 15 years. If you do not like "one in, two out", would you like to see a ratchet effect that says reliefs need to be looked at periodically? The supposition could be that they rise in line with inflation or that they are specifically reviewed to see whether they should be changed, as opposed to being left there pending a periodic review by someone like your own good selves.

Bill Dodwell: We would certainly agree with that. Reliefs should not just sit there forever. They should be looked at both in terms of amount and in terms of whether we need them at all.

We did recommend the abolition of investors' relief. You probably do not know what it is because it is such a rare thing, but it clutters up the statute book. Again, that was introduced by George Osborne. We could not find anybody who supported the idea of retaining it. We said, "Just shoot it, please." That would be a good thing to do.

Q127 **Siobhain McDonagh:** HMRC publishes costs for some but not all tax reliefs. Is the system sufficiently scrutinised?



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Bill Dodwell: More could be done. Since you had your first discussions, HMRC has published a lot more. In January this year, HMRC updated the costings, added more detail in and all that sort of thing, but there is more to do.

In our view, HMRC should gather more data, not less. I know gathering data from taxpayers can be perceived to be a burden, but if you ask people at the right time—when they are doing a return, for example—it is not so hard to have a bit more detail. That would help all of us to understand more about the tax reliefs, the shape of the tax system, the gaps and all that sort of stuff.

Q128 **Siobhain McDonagh:** Following on from a point that Andrea made, HMRC provides data on approximately 200 different tax reliefs. In 2011, the OTS estimated that there were 1,042 reliefs. More recently in 2019, the Office for Budget Responsibility said there were 1,171. Does anyone know precisely how many there are? If not, does it matter?

Bill Dodwell: The NAO is the other body that keeps account of tax reliefs. The number is bigger. I saw 1,190 or something like that from the National Audit Office. Within reason, it does not matter. We all have to recognise that every time we introduce a new tax, such as the plastic packaging tax, which may have perfectly good objectives, we are bound to have some reliefs in the system. The number is going to go up if we take action in that way.

Q129 **Siobhain McDonagh:** Following on from that, many tax reliefs are designed to elicit certain behaviours, such as business investment, saving by individuals or reducing the use of packaging, as you referred to. How confident are you that the Treasury and HMRC are monitoring whether these reliefs continue to have the desired behavioural effect?

Bill Dodwell: I am sure more work could and should be done. I suspect that is a question you should direct to the Treasury, as it is their job to assess the policy of the tax system. HMRC is the operator, so they collect the data necessary and highlight abuses and other things, but the overall shape of the tax system is a question for the Treasury.

Kathryn Cearn: We have pointed out in one or two reports where some of the interactions of taxes and reliefs do not appear to be meeting the policy objective they were originally set for. The classic one in our most recent report was the interaction of inheritance tax and capital gains tax in relation to business assets and agricultural assets.

You do not want people to sell their family business to pay inheritance tax, so they are given relief from inheritance tax when it is passed on within the family. For capital gains tax purposes, the recipient receives an uplift to current market value, but if they are not going to sell it, why do they need an uplift to current market value? There is a relief given that would appear to be contrary to the original objective. If you are not going to sell it, you do not care. If you are going to sell it, would you not be paying the tax on the gain?



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We do point out some of those situations where everybody might agree with part of the objective for doing that, but where there can be behavioural problems. People will not necessarily hand over their family assets until death, when it would perhaps have been better economically for them to hand it over before that, because they are waiting to obtain that relief. That is not necessarily conducive to good economics.

Bill Dodwell: There are a bunch of other ones.

Kathryn Cearn: Yes, there is a list.

Bill Dodwell: There is people buying AIM shares, for example, who can get an inheritance tax relief—business property relief. If you are buying shares on the market as opposed to setting up a company in the first place, you do not need the inheritance tax relief. If you sold the shares, it is not going to affect the business at all. If you are the owner, it clearly does affect the business. You have an issue in that sort of way. We asked the Government to consider what their policy purpose was for allowing that exemption.

Rushanara Ali: Picking up on the points about the abolition of your organisation, you have survived longer than the former Chancellor Kwasi Kwarteng. With Dame Andrea Leadsom and others leading the charge with a rebellion, you may last a lot longer—much longer than anticipated.

Chair: She is being mischievous.

Q130 **Rushanara Ali:** I am not. We might support you too. We have already heard about the great work you have been doing. I was just looking at some of the things you did around inheritance tax as well, for instance.

I wanted to focus on what else, on top of what you have been doing, your organisation could do that would be really valuable in terms of simplification and in terms of looking to the future to make the case for all parties to stick up for you in the act of rebellion that is going to follow soon, I hope. Do you have anything else to add that you could be doing in the next Parliament, whatever colour it is?

Bill Dodwell: That is really an interesting question. We had six or seven areas that we thought would benefit from a review. Could the personal tax return be made simpler in the way it operates? That would be one. That is sometimes known as the self-assessment tax return, which is what you as Members of Parliament probably have to fill in.

Secondly, we could look at tax certainty, including the role of guidance, rulings and clearances. It is really complicated for taxpayers when they do not know the answer. That would definitely be something to look at.

At some stage we were thinking of looking at our savings tax system. That will depend very much on the whole politics of the area, if we are being frank. Our savings tax system is quite complicated, and our pension system is quite complicated, so decisions about that would definitely not just be a matter for any technical body such as the office.



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There are huge and broad implications there, but the office could have made a contribution in both those areas.

Rushanara Ali: I do not know whether this would have fitted into your remit or whether your remit could have been expanded, but you might have been able to do some work—maybe you did—on loan charges, for instance. There were retrospective charges put in place, but there was a scandal in terms of what was going on. Some people knew what they were doing—I am not talking about them—but others who were working in the public sector, such as nurses and others, on short-term contracts were told that they had to be paid in a certain way, which caused major problems. Could your organisation have played a role in something like that? Could you have spotted those or not?

Bill Dodwell: I do not think we could have been helpful in that.

Rushanara Ali: Okay, that is fine. You have listed other areas where the OTS could play a little bit more of a role.

Bill Dodwell: I have more too.

Q131 **Rushanara Ali:** Turning to tax relief and value for money, which is what I want to focus on, the Chartered Institute of Taxation told us that it is vital that accountability for value for money for tax relief is confirmed in practice as well as in principle. Who in Government should be accountable for value for money on tax reliefs?

Bill Dodwell: That should be the Treasury, because that is the body that proposes and introduces tax reliefs. They will need input from HMRC, but it should be the Treasury.

Q132 **Rushanara Ali:** Should there be a particular ministerial lead in the Treasury who should do that? Should it be at Chancellor level or ministerial level in terms of accountability?

Bill Dodwell: I would have thought it was probably at tax Minister level. We have more than one Minister who has responsibility for aspects of our tax system.

Q133 **Rushanara Ali:** From your expertise, what would you say is a proper assessment of value for money for tax reliefs? What would it look like?

Bill Dodwell: First, it is really hard to do. You are looking at the economic benefit we have generated from having a tax relief. Sometimes just getting the data around that is really tricky to do. If you take film tax relief, for example, the original version was something given to individuals. That was exploited; it was problematic.

The current version goes to film companies and is intended to incentivise them to do more film production in the UK. That supports a whole range of jobs. It supports a whole range of investment in physical activities, such as the various studios and all those sorts of things. The UK has become one of the leading jurisdictions around the world for film and high-end TV production.



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Working out what the value added of the relief to the UK is quite hard. If you think about our population and all that stuff, do we have more than our fair share of film and high-end TV work? Yes, we clearly do. It is a big success in the UK.

Kathryn Cearn: We are all used to—you will definitely be used to this—seeing all other forms of Government expenditure put through a value for money test. I am also used to seeing it on the boards of arm's-length bodies. There are value for money tests that are done when we are building a new road or whatever it is we are doing.

Although this might be a bit more complicated than that, the principle sits at the heart of spending in Government anyway, in general. Extending it to the provision of tax reliefs or any element of change in the tax system would seem rational, because there would then be a system around it. There would be not just ministerial accountability but official accountability in what civil servants do, and there would be the potential for that to be examined externally by the NAO, by parliamentary scrutiny and so on.

Q134 **Rushanara Ali:** We have had lots of examples of billions in taxpayers' money being wasted. Some sort of improved mechanism for assessing value for money would certainly be helpful, not just in tax relief but more widely. In written and oral evidence to the Committee, academics from the University of Southampton proposed setting up an office that governs the operation of tax reliefs to ensure value for money and transparency. Do you think that that needs to be done? Would the OTS be well placed to do that, in terms of having a remit like that, as opposed to a new entity?

Bill Dodwell: The Office of Tax Simplification would not necessarily be good at looking at tax expenditures. You would have to have a much bigger office with different people, and you would have to have a range of agreements with HMRC to give you access to data that the OTS does not have, for example.

Q135 **Rushanara Ali:** It is not an area that OTS has delved into in the past.

Bill Dodwell: We have not looked at value for money. We have looked at whether we think something achieves a policy purpose or not. Quite a lot of our reports have said, "We are not sure what the policy purpose of this is. Government should consider what it is and, in making that decision, whether it should keep it or not".

Kathryn Cearn: The other problem with it structurally is that the provision of tax reliefs, as Bill has pointed out, is connected to the relief it is being given for. They are an integral part of the overall system. I am not necessarily sure, beyond NAO-type scrutiny, what a separate office that looks at just tax reliefs would be able to achieve on that basis.

Q136 **Rushanara Ali:** The question is whether there is a case for doing anything in advance. Is there further work that needs to be done in this area?



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Kathryn Cearnys: With any change in tax—be it a new tax, related tax reliefs or changes to tax reliefs—there is a general point about how much work is done up front to make sure that they are done in the best operational way and in the most simple way that they can be. That problem with the Budget cycle, in terms of how much can be done in advance to try to make sure that you have, potentially, the best approach to something before it is out there in the public domain, tends to be quite problematic.

There can be very little scope for discussion after the announcement as to whether something could be made better or not. As a consequence of that, we would argue that sometimes things come out where there has not been enough thought put into what the overall consequences are.

My personal *bête noire*, if you want the things that I dislike the most, is higher-income child benefit charge where you have these unenviable options. You can denounce it completely and not take it because you or your partner are earning more than the relevant amount. In that case, if you are staying at home and not working, you lose national insurance credits and the child will not necessarily get their national insurance number automatically when they are 16. Alternatively, you do a tax return to pay the money back. That might be the only reason that you have to prepare a tax return and you might not know that.

There is more guidance out there now, but you might not know that. You might not need to do that to start with, but then you might have to do it in three or four years' time, when all of a sudden you have gone over the limit and nobody has told you that that is the situation you are in. One can see why it was done from a policy perspective, but, unfortunately, we have ended up in a situation where it is very difficult for taxpayers to get it right. The number of people who have been penalised as a consequence is very high.

Q137 **Rushanara Ali:** Our caseloads are full of it. Can I finish with one more question? This is related to the luvvie tax. We all love luvvies, but it has come up a few times. You mentioned some of the reforms and how that has improved things. The former Cabinet Secretary to the Treasury, Lord O'Donnell, said, "Every chancellor would be bowled over by the luvvies and we'd come away with a film allowance. Nearly all of these allowances meant that...really rich people with smart tax advice paid very little tax, which is, alas, the same today". Do you agree that the Government need firm rules on judging the value for money for tax reliefs? That is one example; there will be others where there are lobby groups that are particularly good at getting their way.

Bill Dodwell: Partly, I think that comment goes back rather a long time.

Q138 **Rushanara Ali:** He is referring to now as well.

Bill Dodwell: A piece of advice would be that Government should be very careful about giving tax reliefs where the benefit of them go to wealthy individuals. The evidence of the past is that that has not worked very well.



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Kathryn Cearn: That is why the change to give the reliefs to the companies that are actually doing the work tends to be a much better approach and has created the incentive for investment in the UK that was intended. One would have to judge whether it is enough, but it is certainly much better structured now in terms of achieving its policy objective.

Q139 **Rushanara Ali:** The OTS was never lobbied on tax-relief-type issues.

Bill Dodwell: No.

Kathryn Cearn: No.

Q140 **Emma Hardy:** Thank you for your open and honest evidence. It is refreshing and I like it, so thank you both very much. I want to talk about whether certain tax reliefs can be abused. This is an open question to begin with. We have had some evidence that certain tax reliefs are being abused. Do you agree that it is a problem?

Bill Dodwell: The old individual film tax relief was definitely abused, yes. We should have had other rules that prevented it, but we did not at the time. Clearly, people were trying to get tax relief for more money than they were spending. That was the point of it. We can all see, instantly, that that is not going to be a brilliant plan for anybody. It is always possible that people benefit from a relief that you did not fully intend to do so.

In a previous life, I discovered one relief that was intended for this group over here. In fact, this group over here were getting it as well, so we decided to tell the Treasury about it and some actions were taken as a result of that. It is always possible that the wrong group, or extra groups, will get something, yes.

Q141 **Emma Hardy:** On 19 December, TaxWatch's acting director Alex Dunnagan pointed out potential abuse of R&D tax reliefs. He said that there had been £1.1 billion in fraud and error over the past three years. There was an example that he gave. He says, "You have a tax adviser saying, 'If you put new cocktails on your menu, that classes as R&D'". He gave another example, which was in *The Times* newspaper: "There was somebody who created a new croissant and said it was research and development". What he describes is people working at the boundaries of where the tax relief is operating. It reminds me of being a parent: they are pushing the boundaries of what is acceptable. Is that what you see?

Bill Dodwell: I always think that it is possible. One challenge is, if you have looked at the small company R&D relief scheme, there is about £5 billion going to something like 76,000 companies, which is about £55,000 per company in a particular year. The problem that presents for HMRC is that the volume of that places a huge challenge on their compliance systems, which is why they are trying to make some changes to do that. I cannot tell you whether they will be effective, but that is the purpose of HMRC trying to do that.



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There is an issue around the quality of some of the advisers in that area. If you talk to any of the recognised professional bodies, they would all be horrified at some of those examples you were just quoting. They would see that as a clear breach of their professional standards and that sort of thing. The biggest single problem with R&D relief is that the definition of research and development is not clear.

Kathryn Cearn: It is not clear in all sorts of other places as well. I am an accountant, not a tax specialist. If you think of the accounting rules over R&D and what you can put on your balance sheet instead of just expensing it every year, they are very prudent. They just say that, actually, most things are not research and development unless you can meet some very stringent criteria about whether you really have something that is going to give you some additional future benefit that you would not have otherwise had. They do not even try to define things in the more subtle way that the tax system was trying to do. Because that definition is so difficult to apply, it gets very grey at the edges and it is difficult to stop people claiming things that you perhaps did not originally intend.

Q142 **Emma Hardy:** That is what Alex Dunnagan said. He said, "You have advisers effectively cold-calling companies saying, 'By the way, you have almost certainly qualified for relief. You should stick in for it'". As I say, the examples given are a new croissant and a new cocktail. Is there a way of designing out the abuse of tax reliefs?

Bill Dodwell: The way you deal with all of that will have to be specific to the relief, obviously. It would be worthwhile looking at the definitions of R&D. I think it is the National Audit Office that has pointed out that the claims implied by the research and development tax credits vastly exceed the measure of R&D that ONS estimates for the UK economy. Part of it is because R&D tax relief, by design, extends to some work outside the UK, but there clearly is a difference and a gap there.

Q143 **Emma Hardy:** You would imagine that, if we want to design out abuse, it would have to be specific for each and every tax relief.

Bill Dodwell: Absolutely, yes.

Q144 **Emma Hardy:** Would that be something that your office would be making recommendations to the Government on?

Kathryn Cearn: We could do. One thing that the OTS has done is to involve consultative committees, where we have brought people in who have particular specialist knowledge around certain areas. That kind of area is something that we would probably bring external experts in to have a look at. For something like R&D, I am guessing that you might end up in a situation where you have to be very specific about what the list is within the context of R&D—you do not try to have a definition; you just say a list of things.

The problem is that everybody will come along and say, "How can you say that it is blue-sky research when you have a list of things already? We might be inventing something that is beyond your comprehension as



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to what we would have done". You can see some of the difficulties there, but we might have at least pulled things back to something a bit more rational that cut out some of the more abusive side of things.

If you want to have an R&D tax credit system, I am not clear that you will be able to tighten it up so much that you can only have what you intended in there because of the blue-sky nature of a lot of what is being thought of. We are talking about croissants, but there are lots of good things that people are doing, of course, in molecular biology and all sorts of things.

Q145 Emma Hardy: My focus is more on the fact that these people are getting a tax relief that I believe is abusing the system, which feels fundamentally unfair. Some of the evidence that we have had around different tax reliefs that were being abused included inheritance tax, which I know you have mentioned already; benefit charge exemption for late-night taxis; and principal private residence relief. Are those ones that you have looked at?

Bill Dodwell: We looked at principal private residence relief—the capital gains tax relief. It is the biggest relief in capital gains tax: I think it is worth something like £30 billion a year, compared with something like the £10 billion or £12 billion collected in capital gains tax. If you were to suggest to the population of the UK that they would have to pay tax on the sale of their house, you would not get elected, would you? Nobody would like that.

Q146 Emma Hardy: It is about the abuse; it is not about the policy.

Bill Dodwell: If you look at the abuse, the changes that we have seen over the last decade have vastly cut out any scope for abuse.

Q147 Emma Hardy: The evidence that we have had is that that is an area of abuse. You are saying that it is not.

Bill Dodwell: I do not think that we saw any significant evidence of abuse.

Kathryn Cearns: We made some suggestions. We looked at it because we were looking at property taxes generally, so we would have made suggestions around tightening it further if we could have seen an obvious way to do it. As Bill says, most of the changes that have taken place have tended to deal with that, so people know where they are in terms of, if they have two properties, which one is their residence and so on.

Q148 Emma Hardy: The Institute of Chartered Accountants pointed to intangibles relief as a tax relief that has been used for tax avoidance. Is that another one that you have been looking into?

Bill Dodwell: We have not looked at that at all, so I do not think that I could make a useful comment to you.

Q149 Emma Hardy: No, that is fine. In your opinion, do HMRC and the Treasury spend enough time during the policy design phase in



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considering how tax reliefs could be abused?

Bill Dodwell: Obviously it is a really important part of what they do. HMRC is really well aware of the fact that people push boundaries or do the wrong thing. One challenge with our tax policy system is that it is sometimes quite hard to get external input at the right time, which is when you are thinking about a policy and the different ways that you might go down, rather than, "Here, we have a policy. Can you talk about the details of it?". That is also useful, but is not necessarily as useful as thinking about the overarching policy design. It is really hard, because of secrecy and all that sort of thing, to get external input in that way.

Q150 **Emma Hardy:** Did the OTS ever carry out work into whether a more simplified suite of tax reliefs would lead to less abuse of the system? Did you ever look into that?

Bill Dodwell: We certainly wrote up stuff in our report suggesting that reliefs were not achieving their policy purpose, which is code for something that was surely not going to do what the Government wanted.

Q151 **Emma Hardy:** Is there, was there or could there be a role for the OTS in looking at preventing abuse of the tax relief system? What would it look like?

Kathryn Cearns: By definition, there would have been. The point that Bill is making is about when you want to do it: is it before something comes in or is it when it is in and it is being reviewed after the first couple of years of it being in place? There are advantages to both. The problem, as Bill has articulated up front, particularly if it is within the Budget and is going to be in a fiscal statement, is that it is very difficult to get input sufficiently at that stage to make it the best designed it could be to avoid abuse.

Sometimes, the argument is that you would want to do a post-implementation review anyway to see whether it is working effectively. At that point, you can try to get the external input to give you some information about how you might then improve it—you can see what is happening in practice, but you can also improve the model that perhaps should have been put in in the first place. You might just have to accept that that is the way you need to do it, but you need to have a system for that to happen on a reasonably regular basis.

Q152 **Emma Hardy:** Do you imagine that that would be a mandatory system in place where tax reliefs are introduced and then—I do not know—annually reviewed or looked at however long after their introduction?

Kathryn Cearns: I do not see any reason why you could not have a general rule about how frequently something was reviewed. Bill might have a different view, but I am not terribly keen on sunset clauses because sometimes it is very difficult to change things at particular points in time.

You could have a regular system whereby everybody acknowledges that, say, within three to five years of a relief coming in or a tax change, there



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should be a review. That could be tied up in a wider review of—if it was capital gains tax relief—an element of the capital gains tax system. If that was happening on a regular basis and everybody got used to that cycle and expected improvements to come through as a result of it, that would be a good systemic thing to do.

Bill Dodwell: One thing that you have had in written evidence from quite a lot of people is, “Please do something for the long term”. If you are trying to incentivise business investment in particular, something short term is ineffective.

The annual investment allowance, which is something Chancellors have played with, is a great allowance but, for goodness’ sake, just keep it at the same level. I am really pleased to hear that we are keeping it to £1 million, which means that, year on year on year, it will be the same £1 million. That will be excellent because people will understand that they will get tax relief if they spend that money. “Am I going to get a bit more if I spend it then?” is really hard for a businessperson to work out.

Q153 **Dame Angela Eagle:** To what extent do tax return softwares simplify the customer experience? You can now get these softwares to help you do your returns that are meant to be updated. It might not be the bespoke advice that you get from an adviser who you pay a lot of money, but, for most people, is that not a form of simplification?

Bill Dodwell: I am not sure that it is, because the most complicated thing is gathering the data for a tax return. For all the tax return software I have seen, you still have to gather exactly the same data. You still have to answer the question of whether it is this type of thing or that type of thing. I recommend it—I use it myself—but I am not sure that it is a huge simplification.

Q154 **Dame Angela Eagle:** Do you think that kind of automation and clever upgradable stuff—despite the fact that, as with any software, if you put rubbish in, you get rubbish out, if I can put it that way—is another way of having a go at simplification from a customer experience perspective?

Bill Dodwell: I would broaden it and invest more in digital systems and the single customer accounts. The OTS has done two or three reports in that area. What is the basis of our system? It is pay as you earn. For most people, that operates automatically and takes off the right amount of tax. There are some errors around the tax code, but fundamentally it does that and collects loads of money. There are lots of areas where we do not have that but could.

We could get banks and building societies that pay interest to send that information to HMRC digitally. They would have to identify the right taxpayer customer, so you would need a digital identifier to deal with all of that. That information would end up straight in your personal tax account and tax would be collected automatically, whether through your tax code, if it is pay as you earn, or by sending you a bill and that sort of thing.



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There is huge scope for getting more third parties to provide more information to HMRC. The work we did showed that taxpayers, agents and data providers were all very happy with that and wanted to see more of it, which was quite an interesting thing.

Q155 **Dame Angela Eagle:** That is an interesting thing.

Kathryn Cearn: That could include people who work for Uber or where they are working for a platform.

Dame Angela Eagle: Exactly, where they might have multiple entries to put in.

Kathryn Cearn: They might not be on a PAYE system, but the information is there that could be gathered for them and could be delivered in precisely the same way, with controls, checks and balances over it.

Q156 **Dame Angela Eagle:** There is a great deal of potential in that kind of thing. One other thing about technology, advancement and where we are at the moment is that our tax base is rapidly eroding. For example, if you look at electric vehicles, all the tax that is raised on the sale of petrol is at risk and will exit.

To what extent do we have a unique chance to redesign our tax system with some of the new taxes of the future to be the big heavy lifters in terms of getting revenue in? To what extent did you do any work, or were you asked to do any work, about a design for future taxes that designed out some of the complications we have in our system?

Bill Dodwell: The things we did for the future was that work on digital systems and getting more into that; having a joined-up tax account with HMRC; and changing our tax year from the ridiculous 5 April to something much more logical. There is a whole range of things there.

Q157 **Dame Angela Eagle:** So it interferes with our Christmas rather than with our Easter—that is what you are talking about.

Bill Dodwell: Yes, it is one of those things.

Kathryn Cearn: It deals with a lot of the exchange of information with other countries, which normally have a 31 December year-end, or occasionally 31 March.

Bill Dodwell: It also deals with the platform and all those things. We were keen, to be honest, to look at things like the electric vehicle revolution and do something for the future. We could certainly have done that. We have not.

Q158 **Dame Angela Eagle:** Are you going to be absorbed into the general Treasury and HMRC policy places? When I was a Minister, they were always advising me about which bits were being abused and how things could be designed out—maybe not looking at the entire gamut of 1,100 tax reliefs, but keeping a weather eye on the bigger ones.



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Bill Dodwell: There is no tax simplification unit, if you like, in either the Treasury or HMRC at this stage. It may be that they will introduce one—you will have to ask them, I guess. If you are asking about our staff, the majority of them have ended up working for HMRC.

Q159 **Dame Angela Eagle:** How many do you have?

Bill Dodwell: We had a total of 14. Some left public service, the majority went to HMRC and some remained in the Treasury.

Q160 **Dame Angela Eagle:** There are nine reliefs that cost over £20 billion a year each. Are you particularly worried about any of those? Some of them are rather obvious, such as the income tax individual allowance. Sometimes reliefs are part of the design, which is clearly not quite as bad, unless you start looking at national insurance contributions, which are slightly more complex. Are there any of those big reliefs that cost that amount of money that you are particularly worried about?

Bill Dodwell: Pensions tax relief is one of the most complicated. It is hugely important, it is long term and we are trying to cater for millions of people with it. In the main, it does a pretty decent job, but there are definite issues around the margins. One that we wrote about was the fact that certain low-paid people who earned less than the personal allowance were not getting the tax relief that others were getting.

Q161 **Dame Angela Eagle:** Once the allowances were introduced, there was a shift that clearly showed, if you analysed where the money was going, that it was increasingly being concentrated on those who are well off and that it had been used as a place to put savings, which was tax-free in a way that I do not think the policymakers expected.

Bill Dodwell: I do not think that it is tax-free; it is tax deferred.

Q162 **Dame Angela Eagle:** It is tax deferred until you claim it.

Bill Dodwell: Yes, because when you take money out, you pay income tax.

Kathryn Cearn: That is one end of the scale, but Bill is quite right to focus on the other end of the scale, particularly if you think about the auto-enrolment situation now. There were a reasonable number of lower earners—

Bill Dodwell: Some 1.4 million.

Kathryn Cearn: They were not getting the relevant tax relief because of, again, a quirk in the system, if you like. That is going to deal with that.

Bill Dodwell: The Government are dealing with that in a year's time.

Kathryn Cearn: Although we have commented on certain aspects of the pension system, something more comprehensive around that would have been quite interesting. There are some structural issues around the impact of the lifetime allowance and whether there should be a



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differentiation between defined benefit and defined contribution schemes in relation to how they are limited to stop excessive relief being gained at a cost to the Exchequer.

We could have looked at something around that and suggested ways of amending the system that would allow people to do their long-term planning, knowing what the restrictions would be and not suddenly making them realise that, if only they had done something differently five years ago, they might not be now in the situation that they are in, because they could not anticipate that. It is causing problems.

Q163 Dame Angela Eagle: There are clearly some unintended consequences of the lifetime pensions allowance, not least for highly skilled doctors and people like that, that I am sure were not intended when it was introduced. What about things like venture capital relief? I was particularly struck, when I was a Treasury Minister, that that sounds like a good thing. If a tax relief is called something nice, people automatically assume that it is working.

I could not get anybody to demonstrate to me that the venture capital relief had done any of what it says it should do on the tin. There were no real attempts to try to look at that and have some kind of research into whether that was the case. Do you think that we should call tax reliefs nastier names, so that people do not automatically assume that they are a good thing because they sound like they are a good thing?

Bill Dodwell: Those are reliefs that, by design, are available only to people with more money. It is only if you have more money that you can afford to invest in a company where you might lose it all—an unquoted company. The Treasury and the Revenue have done some subsequent research on them and their effectiveness; I am not sure that anybody would regard it as conclusively in favour.

Q164 Dame Angela Eagle: It was not conclusive when I looked at it.

Bill Dodwell: There is more, I think, since you were involved with the Treasury.

Q165 Dame Angela Eagle: I would hope that there would be.

Bill Dodwell: We did something more about the administration of it. There were some cases where the relief should have been available, but, because of an administrative quirk, it was not. We made some recommendations about fixing all of that.

Q166 Dame Angela Eagle: What about charitable tax relief and definitions of charities? There are colossal amounts of money hidden away in trusts that are meant to be charitable.

Bill Dodwell: That is for the Charity Commission, as you know, to keep an eye on.

Q167 Dame Angela Eagle: I am aware of that, but these things all impinge on the amount of tax revenue that is available, says an ex-Exchequer Secretary.



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Kathryn Cearn: It is a good question. Also, it is a good example of where there is an interaction between tax, other policy objectives and, in this case, civil society objectives. Whether you have got the boundary right is quite a difficult decision in terms of which bodies you think should have charitable status, and then the tax relief follows it. That is not necessarily always easy.

There are other areas where the interactions between, for example, the benefits system and tax can also be very complicated. We have also talked about the employment tests as to whether you are self-employed or not. That is another area where you get an interaction between employment law and tax law, and they do not really work together terribly well. Those require some political determination about which way you want to go around them.

Q168 **Dame Angela Eagle:** Finally, what about trusts and the establishment of trusts for tax-sheltering purposes?

Bill Dodwell: That is a broad question, as you know. There are lots of trusts that may have a tax implication, but I think you would regard it as completely favourable. For example, if you have a life assurance policy, which is designed to protect your family in the case of your death, it is usually written in trust so it can be paid out easily and there is no inheritance tax on that. I think that most people regard that as a reasonable use of a trust. At the OTS, we said that we should just legislate on that so you do not need a trust at all. That would make life easier for everybody. It would ensure that those people who do not manage to write it in trust get the advantage, so it would help everybody.

If you are talking about the more complicated forms of trust, we never looked at that. HMRC was undertaking a review and we thought that we should not work on that area while HMRC was doing so. I do not think that anything much has happened as a result of that review.

Q169 **Dame Angela Eagle:** I have one final quick question. Are you frustrated that a lot of the suggestions that you made have not actually come to pass?

Kathryn Cearn: Personally, yes.

Bill Dodwell: The country would be better off if you could have adopted more of our suggestions, yes.

Kathryn Cearn: I do not think that we expected everything to be done, by any means, and sometimes the time is just not right and things can happen later when they fit with what else is happening in a particular area. I absolutely accept that, but there were some areas where you were correcting a failure of a policy objective or there was not actually that much cost to just making things a bit more straightforward.

My broader frustration is around the digital side of things and how much ought to be invested to get a really good system in place that taxpayers can use efficiently. It is going to require a reasonable level of investment,



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but there is an awful lot that could be dealt with that would make everybody's administrative interactions with the tax system much better, with that better-designed digital interface.

I am not forgetting those who do not have access to the digital side of things. They need to be catered for as well, but over time, that is likely to recede. To me, that is an area where a really good way of doing things—better investment, better transparency about what is happening around it and better accountability for its success—would make a big difference.

Q170 **Chair:** That is helpful. I wonder whether, Kathryn, you could follow up by dropping us a letter with your "Top 10 things that we will no longer be able to do as a result of us not being what we were before." Would that be possible?

Bill Dodwell: Do you mean the top 10 things that we recommended that have not happened?

Chair: Yes, or things on your list that, as a result of your office being folded into the Treasury or HMRC, you are not able to do but would make the country a more straightforward, prosperous place to do business, as I am sure everyone wants.

Q171 **Anne Marie Morris:** The Committee has looked at cliff edges before and they are well known to you. The most obvious example is VAT, but there are a couple of other property-related ones. Roughly how many of those cliff edges—I am not expecting a precise number—are there in the system? Why do Governments use them?

Bill Dodwell: A cliff edge is simple and a taper or something that spreads the change over a period is less simple. Lots of people talk about the fact that, for example, receiving a benefit is means-tested. If you are below a certain income, you get the benefit, but as your income goes up, the benefit is withdrawn. That leads to a higher-than-normal effective rate of tax—I think it is 55% if you were on universal credit and your income goes up so you lose some of it. That is the challenge with tapers.

The challenge of having a cliff edge, of course, is that you either get 100% or you get zero, and that can be very hard to do. Separately, the Tax Law Review Committee of the Institute for Fiscal Studies is likely to have a look at some of the design challenges and thresholds. I do not think that there is a clear, simple or easy answer, I am afraid.

Q172 **Anne Marie Morris:** If your argument—not on your behalf but to explain why Governments do it—is that it effectively makes it simpler, is that advantage still there with the advent of technology? Is there still a place in legislation for those cliff edges?

Bill Dodwell: I suspect that there probably is in some cases, because it is complicated, even with the aid of technology, if something is withdrawn or whatever over a different pace of income or that sort of thing. I do not think that I can give you a definitive, helpful answer. I am sorry.



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Kathryn Cearn: There are also some questions about, where there are cliff edges, whether they are set at the right place. You can see the bunching up behaviourally as you are reaching the VAT threshold. Is it suppressing people from going above that? The answer to that, though, might not be great. If you are going to keep a cliff edge, the answer may be to reduce it from where it is now—is it £85,000?—to a much lower amount. It would be commensurate with quite a lot of the rest of Europe, for example, to have it much lower.

That would be likely to reduce the suppression of economic activity. Once you are getting up to, “Are you going to be earning £80,000 or £100,000?”, if I go up to £100,000, I am going to have to start charging everybody VAT. That may be seen as more damaging than if you move from £15,000 to £20,000. There might be debates around, “It is right to still have a cliff edge, but where should it be?”

Then you still have all the behavioural issues, even with the tapering system that Bill has mentioned, where people try to avoid hitting a marginal rate that is very high, in terms of money they are losing through either loss of benefits or the tax system, or combined. It can be very problematic.

Q173 **Anne Marie Morris:** On the point about behavioural aspects, for some of these cliff edges, as an individual you can live your life in a different way so as not to hit it, but there are some that you cannot help hitting. Do you think therefore that some thought needs to be given to the criteria? I think that what you are both saying is that there remains, sadly, a place for cliff-edge legislation. Should there be some criteria that make it clear what cliff edges should be trying to achieve, when they should and should not be used, and what the decision points should be looked at when they are being introduced?

Bill Dodwell: There could be a series of principles, absolutely. One can be used for administrative purposes. For example, if you do not have a capital gain and your sale proceeds are below a certain level, you do not have to mention it at all on your tax return. That is a cliff edge—I have forgotten what the number is; my colleagues behind me probably know. If you are just below, you do not declare anything. If you are £1 above, you do. That is for administrative ease and, for me, it is perfectly sensible to have it. Yes, it is not 100% desirable, but nothing is perfect.

Q174 **Anne Marie Morris:** Is there a dividing line between those that are for administration as opposed to those that are trying to impact, determine and nudge behaviour?

Bill Dodwell: Yes, I think so. For me, it lets somebody absorb the cost of losing a relief, or whatever it is, better if it is spread over a certain level of income.

Q175 **Anne Marie Morris:** Maybe, when it is a behavioural one, are we better off using tapers or bands?



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Bill Dodwell: Probably, yes, but, as I say, they are more complicated. They lead to an actual higher marginal rate during that taper period. There is the withdrawal of the personal allowance between £100,000 and, I think, £122,140, and the withdrawal rate is 60%. The effective tax charge on that slice of your income is 60%, which is higher than all our other rates of tax of course.

Q176 **Chair:** That is before taking into account the childcare stopping.

Bill Dodwell: It is, yes.

Anne Marie Morris: Indeed, that is absolutely right.

Bill Dodwell: I completely agree.

Q177 **Anne Marie Morris:** Looking at the alternatives—the bands and the tapering, which you say are more complex—is there anything else we should look at? Of the two, which is simpler?

Bill Dodwell: I do not think that there is anything else to look at. The question is how long the taper period is and therefore what the effective rate of the taper is. The shorter the period, arguably the simpler it is, but the financial impact is much more severe.

Q178 **Anne Marie Morris:** Kathryn, I think you made this point earlier. One challenge with something like this is that somebody who has the ability to pay for advice is going to be better off than somebody who is unable to pay for advice. Do you think that that applies to this cliff-edge situation?

Kathryn Cearn: It can be a problem. There is a broader issue around the general population's understanding of the tax system and the way things work. In an ideal world, everybody would probably be taught a lot more about the tax system, the way you can earn money, the way the tax system will tax it and what the impact will be of that, through school and university. I know that some of that happens, but it is fairly inconsistent and depends on how comfortable teachers are, for example, in terms of delivering that kind of help.

There is a lack of understanding. You will have seen recently in the press about the number of people who HMRC are about to send nudge letters to because they are influencers on TikTok or whatever and have not thought about the fact that they are now earning money that actually, in principle, should be taxed. It is lack of understanding that will take you there, but you cannot get around some of the behavioural things that will happen.

Some people do not even need advice to know that if they are approaching the taper when they would start to lose their personal allowances, in the years when it would hit, it would be better to contribute more to their pension to take them down. Then, if you are lucky to start earning enough that you are above that, you do not have to worry about it quite so much anymore, because you missed that gap. People who can just do the maths, to be honest, can understand it. Any



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good tax adviser would advise it, but a lot of people will tend to be able to see that anyway at that level.

The more that people understand the tax implications of what they are doing, and the better informed they are, the more likely they are to do things the right way, which means compliance, and to be able to anticipate it. They will know that, when they start earning that level of money, particularly if it is not PAYE, they need to keep some money back to pay the tax. That is incredibly important and why some people who are in gig economy jobs really struggle—they cannot cope with the cashflow implications.

There is a lot that could be done around education and, as we have talked about already, whether people in the gig economy could opt into something that looks a bit like a PAYE system, so that they get taxed on a more regular basis, rather than having chunks taken twice a year. There are lots of options around that to make things easier for people.

Q179 Anne Marie Morris: I have one final question. You made an interesting point that where you set the cliff edge is as important as the mechanism you have chosen—that is, whether it is a cliff edge, banding, tapering and so on. You made the interesting suggestion that, if you set the figure lower for VAT, it would become less of a problem because more people would be caught, and it would be in your psyche at the time you were setting up your business, because you had already thought that you would get beyond that point. Is there any advice that you think Government should have about how they decide what that figure or level is? You are telling me that it is crucial to get that right.

Bill Dodwell: If you take the VAT thresholds, Governments of the past thought, “Let us focus on administrative saving and making life simple for an individual being self-employed and that sort of thing. Let us just put the threshold up”. They never thought enough about the impact for growing businesses in going through that threshold.

More recently, Governments have clearly had that in mind, which is why the threshold has been frozen and we have seen, as Kathryn referred to, the bunching below that. The *Financial Times* published more evidence of even more bunching below. It remains a challenge to deal with.

Kathryn Cearns: Also, do not downplay the political challenge of suddenly saying, “Actually, do you know what? We are going to do something different with the thresholds”. It is such a long-standing thing. You have the drag effect of leaving it frozen and not raising it in line with inflation, but I do not think there has been that much work done about how much you want to encourage businesses to grow at that level.

How much is it really stopping people? Do they stop, stop, stop, bunch and then realise, “Actually, I am being so successful that I have to take a grip and do it”? Do people just sit there all the time and consistently say, “That is enough money for me to earn. I can avoid having to deal with VAT. I will just stick at that level,” when they could easily do more if they



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did not have that disincentive? It is that kind of subtlety and work that would probably need to be done to look at that. Changing something that is very embedded is always going to be a challenge.

Bill Dodwell: If you wanted a principle, any of these thresholds, cliff edges or whatever ought to be reviewed every five years. There may be no changes made at that time, but there should be a process of formal review. What seems to happen is that things just sit and ossify. The OTS recommended the abolition of luncheon vouchers. They were hugely important in the 1950s, but three shillings or whatever it was in the 1950s was a whole meal and 15p, when they disappeared, was absolutely nothing at all—it could not even buy you a chocolate bar.

Q180 **Chair:** They are not still there, are they?

Bill Dodwell: No, they have gone.

Q181 **Anthony Browne:** All Chancellors want to simplify taxes, or at least they say they do. You might imagine a Chancellor coming in and saying, “I am going to simplify taxes by simplifying the whole relief system, not creating new ones and getting rid of some old ones”. They might do something like set up the Office of Tax Simplification, but we will not go down that route. With over 1,000 reliefs there, how would you design a process to, first, filter out new reliefs that do not make sense and, secondly, to simplify the reliefs we have in a rational way?

You could not do a random thing and say, “We will go for that one because it is high profile, or that one”. You have to have a more evidence-based system than that, which first stopped new reliefs being created that should not be created. You talked earlier about the asymmetry. People such as Ministers go and meet luvvies and they then come out with a film tax relief. That will always happen. You cannot stop that, but is there something about designing taxes, process-wise, where you could make sure that new reliefs are not created with such abandon, as they are at the moment?

Bill Dodwell: It is down to a lot of different things, all of which sound relatively small, but combined have the effect that you are after. First, it is trying to establish an evidence base around that. That requires some detailed research into the industry, business or whatever it turns out to be. We could do more of that. We need to ask whether we should have a grant system rather than a tax relief. If you are to have a grant relief system, do you have a body that could administer those grants suitably?

For example, we have a theatre tax relief and an orchestra tax relief. These are both small, trivial annoyances. We have an Arts Council and all that sort of thing, so why did we not just give them the money? There are apocryphal stories about why we ended up with what we did, but they are not great uses of the tax system.

Q182 **Anthony Browne:** A Minister met somebody who played in the orchestra.



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Bill Dodwell: It was probably something like that. They are too small. Individually, if a theatre gets £500,000, that is great, but that is for the Arts Council or something like that, I would suggest. You need to look at grant-making in general. We have tax reliefs as opposed to zero rates of tax on bands, which sound the same, but actually are classified differently. That is another part of it.

Q183 **Anthony Browne:** What is the difference between a zero-rated band and a tax relief?

Bill Dodwell: It is because it is not a relief. It makes no sense, but people count reliefs as where you get some money off, as opposed to having some of your income taxed at nothing. Do not ask me to justify it because you cannot, but they are looked at slightly differently.

Kathryn Cearn: They are looked at differently in the fiscal system and I think in the ONS system as well. The design can be very similar. The other issue, which we have discussed already, is that, if a relief is introduced because a new tax is being introduced and it is attached to that tax, does it fit in with the overall policy initiative of the introduction of the tax, in terms of driving behaviour—for example, the hope of getting rid of plastic packaging? What reliefs are you giving in relation to that and why?

That is probably a bad example, but sometimes reliefs are given for small businesses. Actually, when you accumulate all the small businesses together, they may be creating worse problems than some of the bigger businesses. There is a question mark there over what you are trying to achieve in aggregate from the tax policy driver. Is the relief helping that or hindering it? Is it a transitional relief to let these people into a more costly regime, so that it builds up to it and is going to disappear anyway? In that case, you can build that into the structure when you initially start it.

It is mainly about whether you can question at the right time whether the design is right. Is it meeting the policy objective? Then, as Bill says, post implementation, you have to review it to see whether it is actually doing that. Is it more costly than we thought? Is it not actually driving the right behaviours? What is successful and not successful, and should it therefore be amended?

Q184 **Anthony Browne:** I am showing my ignorance of Treasury internal mechanics, but does it not go through a process at the moment when it designs the tax system or a relief to check that it has an evidence base and pursues the policy objective, and that there is a post-implementation review? Effectively, you are suggesting that there should be more use of internal working guidance and for each tax relief to go through this process.

Bill Dodwell: There is not a huge database available where the Treasury and its officials can suddenly say, "What evidence do we have on this?" They go to KAI, which is the knowledge, analysis and intelligence part of HMRC, which keeps the statistical data and presents all that. It asks for



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analysis, behavioural effects and all that sort of thing, but sometimes the data is just not available, or it is not the best data. Sometimes, the view of behavioural aspects is not well understood by HMRC and is better understood by people outside the organisation. Yes, it tries, but it absolutely does not have enough to help to design the best system.

Kathryn Cearns: Also, if you compare the system for the development of changes to the tax system with the way that other Government legislation changes, you do not have all that build up to actually implementing it and putting the law in place. You do not have the consultations and the external input that can come from them, the analysis, or the ability to take some time to look at some of the likely impacts and get external input into that. You are going to announce it on Budget day and quite a lot of it is effectively a secret until then. That is why, being realistic, the post-implementation phase is probably more important in terms of making sure that things are reviewed and not just left as they are.

Q185 **Anthony Browne:** You are absolutely right, but the trouble with that is that it often might be too late—they will not want to take it away again. We might do a post-implementation review of the orchestra tax relief, but they do not want to be accused of being anti-musician or something similar.

Kathryn Cearns: People would need to get used to that rhythm of review and knowing that it was going to be looked at again—

Anthony Browne: They would know that it could just be temporary.

Kathryn Cearns: It is not even that things are temporary, but, “We are going to check that it is doing what we thought it was going to do, at the very least”. Everybody would get used to that, particularly if they then saw a pattern of quite a few of them staying because they were doing what they were designed to do. There would also be variations on that where some things that were not working had to be tweaked and some things that might cause them—in rare circumstances, I hope—to say, “This is not working at all. We need to do something different”.

You want to be careful around getting that cycle well understood because of the stability issues, where people are taking quite important economic decisions based on what they expect to happen and then it gets withdrawn. If these are very long-term things, that can be problematic. You have to be careful about it.

Bill Dodwell: When Jeremy Hunt took over, or previous Chancellors, he will have said, “I have a Budget coming up. These are my ideas, together with my advisers and possibly Number 10, of things I would like to do.” That is where the impetus comes from. Officials then have the task of trying to see how that turns into a workable policy. Do we have any evidence for or against those things?

We must not underestimate the political initiative and the relatively short time that gives to put together that policy. Few Chancellors think to



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themselves, "In two years' time, I would like to do this", and go out and find a method of doing it. They are all thinking about the next Budget.

Q186 Anthony Browne: We touched earlier on Lord O'Donnell's comments that Ministers would meet luvvies and come up with a tax relief, so you end up with a tax relief system where the very rich who have good advice end up with better reliefs. Clearly, it is not a good way to design tax reliefs, in terms of people who Ministers meet or people who have well-paid tax advisers. Is there a way that you could make the system fairer for all taxpayers?

Bill Dodwell: Bodies such as the OTS, I would hope, would think about all taxpayers. Our focus, as Kathryn said at the start, was on individuals and nano or microbusinesses. They are the ones who need most help and there are many more of them than multinationals, which, arguably, need less help. Yes, you can do that.

Take a recent example: our last report was on hybrid and distance working, which is a big topic in the UK and internationally. We did not have time to produce recommendations. Instead, we listed the requests from business for tax reliefs, which was a long list. If we had done recommendations, frankly, we would have done it a bit differently. We would have evaluated what was more and less valuable. As it is, there is stuff to be done there and I hope that that work will be taken up by the Treasury and HMRC. We could have done some of that if we had had more time to do so.

Q187 Anthony Browne: We have had some evidence from academics at the University of Southampton that tax reliefs can increase not only income inequality but regional inequality. The R&D tax relief benefits the south-east, in particular my constituency of South Cambridgeshire—thank you very much. Clearly, Government policy should aim to promote growth across the whole of the UK. How can you make sure that tax reliefs are fairer from an income equality point of view, but also regionally?

Kathryn Cearn: It comes back to the point that Bill made. If you want to encourage specific economic activity in specific parts of the country, you can require people to be based there and have their activities there. You can do that through the tax system or through grants. If you are doing it on a national basis, you are not telling people where to put their factory, research facility or whatever. You can always try to direct it that way.

I am afraid that my attitude to what they have said is, "That is a reaction to where the bulk of the economic activity is." If you just do it on a national basis, that is what is going to happen. There are research facilities in other places. Some of them are attached to public sector land. I am on the board of the Nuclear Decommissioning Authority. Some of our sites are being decommissioned and they are building research facilities there. They are in lots of different parts of the country. There are different ways of motivating geographical investment that can be done on a more nuanced and regional basis.



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Bill Dodwell: The economic evidence for the effectiveness of things like investment zones is quite doubtful.

Chair: That is in terms of the UK overall.

Kathryn Cearn: You need a lot of infrastructure to run a business around you—you need a certain type of workforce and all sorts of other things to make it work. That is part of the problem.

Chair: The Committee had wanted to have you in early this year, which is why we have got you in on 1 March. We had wanted to hear your evidence, given that Chancellor Hunt has not reversed the decision of his predecessor to end the Office of Tax Simplification. We have certainly heard very clear evidence from you today in terms of what you have done. Both of you feel that this is an unfinished agenda. That clarity has been very helpful to the Committee.

Thank you not only for your evidence this afternoon, but for all you have done to contribute to the office over the years. I recommend that our Committee take this away by writing to the Chancellor to find out the justifications for why he has continued with the ending of your separate existence, so that we can then consider what our next steps might be as a Committee. I want to thank you very much for your service.