

Treasury Committee

Oral evidence: Budget 2017, HC 1069

Tuesday 18 April 2017

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Members present: Mr Andrew Tyrie (Chair); Mr Steve Baker; George Kerevan; Kit Malthouse; Chris Philp; Mr Jacob Rees-Mogg; Rachel Reeves.

Questions 172-249

Witnesses

I: Chas Roy-Chowdhury, Head of Taxation, Association of Certified Chartered Accountants; Bill Dodwell, President, Chartered Institute of Taxation; Nick Parker, Deputy President, Institute of Chartered Accountants in England and Wales.

Examination of witnesses

Witnesses: Chas Roy-Chowdhury, Bill Dodwell and Nick Parker.

Q172 Chair: Of course this hearing no doubt would have led the bulletins, were it not for the fact that the Prime Minister has decided to make a statement, which we gather is already heavily leaked all over the press, that is likely to supersede the further work that will be undertaken. On previous form, when an election is called, at that time large sections of the Budget are excised in hurried negotiations between the two Front Benches and a concertina'd Finance Bill is pushed through on an agreed basis in order to ensure that the public finances are not put at risk. It remains to be seen exactly what will happen but it will have a big bearing on what this Committee will want to do in the remaining days, were this announcement to be correct, which we still have not formally heard but it looks as though it may well be. Therefore, those intending to appear before the Committee in meetings that we have scheduled subsequently will need to contact the staff to find out what, if anything, is likely to be happening.

I begin with one very simple question before we get into some detailed issues: how does this Budget and its accompanying Finance Bill measure up against this Committee's principles of taxation that it set out in the last Parliament and that have been endorsed in this? Perhaps I will move from left to right as I am looking, partly because Bill Dodwell is a very experienced and seasoned campaigner here.

Bill Dodwell: Good morning. The Finance Bill is the product of Budget 2016 and other additional work; we give it a low score at the Chartered Institute of Taxation because of its massive length and complexity. We give the actual Budget, the Spring Budget, a higher score, partly because there are very few new measures—obviously we will talk about the controversial measure, the national insurance one, but the other measures were not great surprises—and it probably meets your scores, so we would give the Finance Bill a much lower score. We give it six out of 10 whereas we give the Budget seven or eight.

Q173 Chair: That is not a much lower score. Six to seven sounds like pretty much the same score.

Bill Dodwell: Ah well.

Q174 Chair: You are a very cautious man.

Bill Dodwell: There has been a fair bit of consultation on the Finance Bill and we should give the Treasury, HMRC and the Government credit for that consultation. But the problem for many of us is the massive complexity of it, and the fact that it is adding more pages to the statute book than any other Finance Bill before it, and the next one is Finance Bill 2012.



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Q175 **Chair:** Still you score it six. What do you have to do in order to get a score lower than six?

Bill Dodwell: You have to produce much less consultation in advance—that is the saviour of the Bill.

Q176 **Chair:** If you consult a lot about something hopelessly complex, you will still get a reasonable score in the Dodwell world.

Bill Dodwell: In the Chartered Institute of Taxation world, yes.

Q177 **Chair:** Okay. Mr Parker?

Nick Parker: To some extent we would agree with CIOT, except we would mark the Finance Bill lower because of its complexity and unnecessary complexity.

Q178 **Chair:** We are asking you to mark it.

Nick Parker: I would probably mark it at four.

Q179 **Chair:** Okay. Mr Roy-Chowdhury?

Chas Roy-Chowdhury: Yes, Chairman. The Finance Bill and the Budget taken together as one unit is hideous: 776 pages, 270-odd pages on interest and loss-relief restrictions. I would be hard pushed to give it three overall because of the extreme level of complexity and unnecessary complexity in many cases that has been brought into the tax regime and the tax system. It needs to be rowed back; we cannot have an ongoing situation where we have the Office of Tax Simplification at the one end trying to simplify and the Government at the other end trying to make the tax regime as complex as possible. There must be a point at which it just becomes “enough is enough” and we start rowing back on this.

On this Finance Bill, a number of measures have already come in from 1 April that have not even been enacted. We do not know how the law is going to sit. From looking at your six principles in terms of legal clarity and simplicity or targeting, I just do not know which benchmark, which target, is satisfied in terms of your six principles from the Treasury Select Committee. It warrants a very low score.

Q180 **Chair:** You were offering lower than three a moment ago. The number below three is two.

Chas Roy-Chowdhury: That is right; I would say between two and three, and I would say three to be generous, as there is so much retrospection in terms of the Draft Bill.

Q181 **Chair:** Where has Mr Roy-Chowdhury got it wrong, Mr Dodwell?

Bill Dodwell: There are some corporate measures in there, limits on interest deductibility—this has been part of the OECD/G20 Base Erosion and Profit Shifting Project. The papers were announced in October 2015; the Government said immediately that they wished to enact that at the first possible opportunity and have sort of carried on down that path.



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Quite a lot in business have said, “Hang on a minute—the UK is going well ahead of other countries in Europe”, and therefore ahead of other countries globally, because Europe is ahead of everywhere else in adopting that, and have asked for a deferral. The complexity of it warrants the deferral, but the response from the Treasury and the Revenue has been that there is a lot of money involved here—it is about £1.2 billion a year, which is about 5% of the annual corporation tax paid by large companies, and that has underpinned the Government’s point. It is fair to say that the Revenue have consulted very extensively, they have taken on lots and lots of detailed points, and they have made quite lot of changes.

Q182 Chair: The complexity is your fault: you have offered all of this complex advice in response, and they have delivered an even more complex Finance Bill.

Bill Dodwell: I partly accept that criticism. The problem comes where you have something that is intended to apply to a complex corporate world, particularly an international corporate world, and at the same time you are trying to make sure it is fair and does not have unintended consequences. If you simply had a flat rate and said, “No interest above this would be deductible”, that would be simple but it would not be fair, and that is why we have got the exceptions.

Chair: We have given the chartered institute a double whammy there. I am going to move on though.

Q183 Chris Philp: I would like to turn to the question of business rates and I would like the panel members to start by offering some general comments on the impact they think the business rates revaluation will have on businesses, concentrating particularly on small businesses.

Bill Dodwell: Firstly, I should say this is not an area where we claim significant expertise, and I understand you are at least due to hear from people with more expertise later. If you look overall across England—because of course business rates are devolved to Scotland and Wales already—there is only one main region affected, which is London. Other parts of other regions are going to be affected, but overall the other regions probably face reductions in business rates, rather than increases. The most important challenge here is that, particularly in higher valued places, partly caused by the delay in the valuation—we deplore leaving it for seven years, which is what has happened—you have got a lot of businesses that have seen their premises move out of exemption into rates, and the attempt here from the Government is to smooth a path as you move from exemption into paying business rates. I think you will find others will probably say they have not been completely successful in what is coming forward.

Chris Philp: Who else would like to comment on this generally before I ask a couple of specific questions?



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Nick Parker: There needs to be a wider review. As we all know, everything has changed with regard to the high street; you have got out-of-town shopping, you have got internet shopping, and perhaps there needs to be a wider review generally of how this sort of funding is made to acknowledge there has been this change.

Q184 **Chris Philp:** Given the change you are referring to—the growth in particular of internet shopping, which relies on a very few number of large warehouses that are relatively cheap and have, relatively speaking, low business rates—how would you suggest the Government consider fundamentally reviewing business property taxation or business taxation more widely to address the point you have referred to?

Nick Parker: It should not necessarily be just focused on the high street, where the values are; this is where there needs to be wider consultation. I am not an expert in this area, but there clearly needs to be a rebasing with regard to business rates and business activity to acknowledge this and make the system fairer, because I do not believe it is fair at the present time.

Q185 **Chris Philp:** Tangibly, how would you recommend that might be done?

Nick Parker: The simple answer is I do not know.

Q186 **Chris Philp:** Mr Roy-Chowdhury, do you have any suggestions on that point?

Chas Roy-Chowdhury: The system at the moment cannot be fair. You get large businesses, say Tesco, who are winners overall because of the mix of businesses they have. Small businesses—which, as you quite rightly say, are concentrated in urban areas such as the South East—are going to be losers because of property values. I just wonder if there is a way of disconnecting property values from business rates so that you do not have this sort of constant lottery. At the moment, the South East property values are more stable and other regions are going up, so you are going to get problems down the track. Do we need to have a business rate that is so directly related to property value? I do not know what the answer is and, like Nick, I do not know if we ought perhaps to be looking at some sort of local tax. I do not know what the answer is, but clearly it cannot be right to have a situation where small businesses are being thrown out of business or are seriously having to reconsider what they do because of the rating values that are coming in.

Q187 **Chris Philp:** Within the context of the existing framework, would you agree with the comment we previously heard that, if we are going to have a value-based system—accepting that we probably should think more broadly about something that is fundamentally different—we should have much more frequent revaluations?

Chas Roy-Chowdhury: In the consultation, that is one of the options. Under the self-assessment system there are options of revaluing quite frequently, but I understand the local authorities cannot handle that so



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they push back on how frequently that can be done. At the end of the day, it means that incrementally costs are going to go up unless you do something about the property-value-based system, so we need to look at that.

Q188 Chris Philp: But you do not have any specific proposal for how we might handle it differently.

Chas Roy-Chowdhury: As I said, maybe there is room for some sort of local tax on business rather than based on property value. I do not know what the answer is, but we cannot end up in this situation again.

Bill Dodwell: The only thing I would add is that Scotland has looked at a local tax and decided against it—that it would be too complicated and would not achieve the result they were looking for.

Q189 Chris Philp: Thank you. I have two more specific questions on the current system. The Government announced in the Budget £435 million of support to alleviate the impact of business rates; that will fall mostly in London, because that is where business rates have gone up. But if I look at the profile of that spending over the next five years, it is largely front-loaded; it is loaded into the financial years 2017-18 and 2018-19 but, because of the transitional reliefs, the business rate increases will not really bite until 2019 onwards. Would the panel share that analysis and would the panel agree that the Government should look again at the profiling of that spending so it is more loaded towards the later years rather than the early years?

Bill Dodwell: I agree with that point, yes. Either you need more support or you need to change the profile of it.

Nick Parker: It needs to be smooth.

Chas Roy-Chowdhury: That is right. You need to tie the support with the actual increase rather than having it before the increase occurs.

Q190 Chris Philp: You share my worry that the £435 million is loaded in the front two years when actually the protection of transitional reliefs applies most. Okay—the panel are all nodding.

Secondly, somebody mentioned—I think Mr Roy-Chowdhury—the unfairness that Tesco, for example, or large supermarkets are in some cases effectively getting a business rate cut, because they have large premises, the values of which have purportedly gone down. In fact the UK's largest business rate payer, Heathrow Airport, is getting a business rate cut. One way of fine tuning that would be to have in the transitional reliefs a zero downwards floor for large business—that would be defined as businesses with a rateable value over £100,000—which would then finance more generous upward caps for small businesses, which are currently 5%, 7.5%, 10%, 15%, 15%. Is that an approach that would have the panel's support?

Chas Roy-Chowdhury: I think that idea was floated before the Budget.



Q191 **Chris Philp:** It was floated by me but not picked up.

Chas Roy-Chowdhury: Okay. It certainly does, if you like, redistribute from the big businesses, which win out, to help small businesses specifically. That might be a way forward, but rather than a sticking-plaster approach, we need to have a root and branch look at how business rates currently stand and whether we do move to a local tax or whether we do just take the property value out of the way that rates are set.

Q192 **Chris Philp:** I accept it is a sticking-plaster solution, but it will take some years to do the more fundamental reform. Are there any other comments on that?

Nick Parker: Given the current system, yes, I would agree with you: that would be a fairer way of distribution.

Bill Dodwell: The only challenge is that if you want a business rate to be based on a property value, constantly deferring that through transitional adjustments has a higher disconnect between what the business is paying and the transitional value. It would also have an effect on businesses moving from one property to another, for example, where I assume, if you went to a new property, you would not get the transitional relief whereas you do while you are still there, and so that has another impact on upsizing or downsizing or whatever.

Q193 **Chris Philp:** That is right. The transitional reliefs do not apply to a property; they apply to the occupier of a property, and if they move the transitional reliefs disapply.

Bill Dodwell: Again, I will not claim enough expertise on this; I thought they were linked to both.

Chris Philp: That is a very interesting point. Thank you.

Q194 **Rachel Reeves:** Thank you very much for coming in to give evidence to us today. The Budget itself and the immediate aftermath was pretty chaotic, to say the least, but the Prime Minister and the Chancellor were pretty clear that national insurance would stay at its current levels through this Parliament. Obviously we are now aware that this Parliament is coming to an end rather sooner than many of us had thought. Would your assumption be that this issue of raising national insurance for self-employed workers would be back on the table if the Prime Minister were to win the General Election in June?

Bill Dodwell: Firstly, you are tempting us into a political comment and I would rather duck and weave on that one. On the economic point of whether we should tax similar forms of work in a similar way—and by tax I include national insurance—our view at the Chartered Institute of Taxation is yes, we should, and having big differences between the two is not helpful because it obviously encourages businesses and others to migrate towards the lower tax outcome. We did understand, though,



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that when the Chancellor made the proposal in the Spring Budget, that was perhaps the least obvious time to have made it; obvious times would have been when the state pension increase was announced for the self-employed, or when the abolition of class 2, the flat rate, was announced, or after Matthew Taylor delivers his report to Parliament.

Q195 **Rachel Reeves:** You would be supportive of a manifesto that had in it an equalisation of the tax and national insurance treatment of—

Bill Dodwell: I do not think we would go as far as equalisation, because there are clear differences in employment rights and worker rights; there are also differences in risks, and one of the questions is: should the economy as a whole, should the Exchequer, help people bearing some of those risks? Our view is possibly they should, although I know economists will probably disagree and think that it is all dealt with through price, but we do not think it is easier to deal with that through price. No, we do not think everyone should pay exactly the same, but we do think the gap has got too large.

Q196 **Rachel Reeves:** Where would you see the balance lying, Mr Dodwell?

Bill Dodwell: If you look at the benefits that people get, the state pension is of course the biggest single benefit any of us earn through paying national insurance, and given that has now been equalised or is for the future, that deals with much of the difference generally. Certainly moving national insurance up would make that easier to deal with. The challenge, of course, is that certainly for the last 20 years and certainly since the abolition of advance corporation tax by Gordon Brown in 1998, we have seen a sort of increased focus into sole workers or very small businesses using companies instead of partnerships or self-employment, because there have been lower taxes coming through that. In trying to deal with that, no one has found a great answer.

Q197 **Rachel Reeves:** Would you like to come in, Mr Parker or Mr Roy-Chowdhury?

Nick Parker: We were surprised at the timing of the announcement, given that the Matthew Taylor review is under way. We thought it would have been much more sensible to have left it for the review to have taken place and then perhaps provided a complete package following that review, which may indeed have included an increase in class 4 national insurance. We would agree with Bill that in fact there needs to be a complete review looking at employment law, benefit entitlement and tax; it should not just be isolated. There needs to be a complete review of the taxation of employees and the taxation of the self-employed, because there are anomalies throughout the legislation. We would agree that there needs to be a review and we would expect class 4 national insurance rates to come up, particularly for the reasons that Bill outlined.

Chas Roy-Chowdhury: Bill and Nick have both covered it, but it seemed very odd to announce an increase without the Matthew Taylor review coming out. We should wait for that. In terms of the principles



behind raising the national insurance class 4 contributions for the self-employed, can there be an equalisation of benefits—clearly maternity leave, paternity leave, unemployment benefit? How are you unemployed if you are self-employed? There can probably not be a full equalisation, and on the other side you are not getting the employer's contributions, so you are going to lose that anyway. I guess you could say that if somebody is self-employed, there is no employer's contribution, but there probably needs to be at least some degree of understanding that the individual going into business is taking a risk. They do not have job security in the same way as somebody who is employed, so we do need to keep that in mind in terms of any equalisation that happens.

Q198 Rachel Reeves: Isn't the biggest difference between being self-employed and an employee the employer's national insurance? if you are earning average earnings, just over £26,000, if you are an employee then your employer pays £2,500 national insurance, and if you are self-employed, there is no employer so there is none paid. Isn't the incentive to encourage people to go self-employed not necessarily with the person who becomes self-employed but the person doing the employing? These changes to national insurance for the self-employed will not change that incentive on the part of the person doing the employing, whether they are employing a self-employed person to do work for them or directly employing somebody. How can you change those incentives, or is that just not possible?

Chas Roy-Chowdhury: I do not think you get the individual to pay the employer's contribution, because that will just make it uneconomic to go into business, so you cannot deal with that and you cannot expect that individual to pay that. At the same time, we need to recognise that those who are employees probably do not feel the pain of that employer's contribution. Somebody who is self-employed equally should not necessarily be penalised for that. At the end of the day, NIC is a part of general taxation, so we need to recognise it for what it is and we need to then see whether we do something additional around taxation to cover that additional cost. Going back to Nick's point, we probably do need to have a more fundamental look than just purely looking at employment and self-employment as the nexus for the NIC payments.

Q199 Rachel Reeves: I understand your response, but the point I am getting at is that companies like Pimlico Plumbers, Deliveroo and Uber have been taken to court over their employment practices by workers saying, "Actually we are employed by you; we are not self-employed". The incentive for those companies and many others is that they do not have to pay the employer's national insurance but also they do not have to pay holiday pay, sick pay and all the rest of it that you get if you are directly employed.

Bill Dodwell: Can I make a point? Presumably the amount that is paid is higher to reflect the fact that some of those sorts of benefits that would be taken by an employee are not necessarily directly taken as a



self-employed person. Those cases—as I am sure you know—are about employment law rather than tax or national insurance law.

Q200 Rachel Reeves: Yes, but if you look at why the employers are encouraging people or changing their business models so that people doing the work for them are self-employed, that is not just because of the employment law. The Government's whole point on the changes to national insurance was that they were losing out on tax revenue and national insurance revenue because the nature of the labour market is changing. The point I am making is that just changing the national insurance for self-employed people, many of whom are low paid and on average are lower paid than people who are directly employed, clobbers them with a higher tax bill but does not do anything to change the incentives of those companies that are changing the nature of the labour market either to get out of employment rights or to pay a lower effective rate of tax.

Bill Dodwell: You have a number of different points tied up there. One is to look at the boundary, and of course there is a measure in the Finance Bill such that when public bodies engage workers through companies, the public body or the agency must test whether this is a quasi-employment or self-employment. If it is a quasi-employment, the public body or the agency must deduct Pay As You Earn and must pay employer's national insurance. Dealing with the boundaries is a really important thing, and many of us expect that at some future date a government will look at extending that to the private sector. It is complex, it is not perfect and there are implementation issues, but you can see why we should not have boundaries used because of enforcement.

You also have a second point: if you look at a continuum between the self-employed plumber on his own, the tradesmen generally, the garage mechanic and the corner shop, you then have the freelancers who provide their labour, and then you have the employees. I would suggest the question really is about those people in the middle—the freelancers. How do you properly characterise them?

Q201 Rachel Reeves: Do you think Government could do more to iron out some of those ambiguities?

Bill Dodwell: Yes. Ultimately it would be a sensible plan to legislate for the difference between self-employed people and employed people. I hope we will see that in years to come; it will not be easy to do, but we rely on a series of tax cases over the decades. They are sort of distilled into various practices and into an online tool from the Revenue, but it is not the best answer. We need a bit more clarity.

Nick Parker: There needs to be greater clarity on who is truly self-employed and who is truly employed. That is the fundamental issue and that is where we need to get to with a proper review, because we have all seen people who are regarded as being self-employed who, if



you look at it, probably are not self-employed. That is the fundamental issue.

Q202 Rachel Reeves: Would that be a more successful route for the Government, bringing in the tax revenue that they think they are missing out on, than simply increasing the national insurance contributions for people who are self-employed?

Nick Parker: Yes, because there needs to be this whole review with regard to it so that everybody can understand where the boundaries are, and that would be much more palatable for the public as well.

Chas Roy-Chowdhury: It is about broadening the tax base, and with the gig economy, that is going to be more and more the case, where you have this quasi-employment situation, and we do need a solution—one where the business and the individual knows where they stand.

Q203 Mr Steve Baker: Another issue on which there is a spectrum of opinion—even, dare I say, perhaps on this Committee—is the tax-free dividend allowance. Last year the OBR's assessment of the new dividend tax was that there was a forestalling to the tune of £800 million. How do you think the Government ought to strike the right balance between high-quality consultation and this problem of forestalling?

Bill Dodwell: It is an incredibly difficult thing to do. When you make a big structural change, such as with the change of dividends, it is very hard indeed to prevent forestalling, prevent people paying it, and the most important thing, I would suggest, is to end up with the right system at the end of the day. That is the system we then have for the next decade or two, and worrying about whether somebody saved some money in the very short term is arguably less important. It is very difficult to deal with that with a structural change.

Q204 Mr Steve Baker: That is a very interesting point. Since you raise it, I am just looking at the costings of the policy, and £870 million was the increased revenue to the Exchequer for 2019-20, and in 2020-21 it was £825 million. This forestalling looks like an entire year's worth of benefit to the Exchequer. The question really to you is: do you think that we get the benefit of tax stability for 20 years, as you have perhaps just suggested we might?

Bill Dodwell: It is too hard to tell the answer to that particular question. We saw this with the introduction of the 50% tax rate and then its abolition, and obviously that had impacts as well. It is very difficult, when you make such a big change to the system, to just come out with an announcement that it applies that day and there you are. You can arguably say that, with the forestalling, what has happened is people have paid tax earlier at a lower rate; they might well have paid that tax, as you rightly say, over the next 20 years. We just do not know how that realistically would have happened.



Chas Roy-Chowdhury: You could transition it in, but then again you are against your principles in terms of simplicity. It clearly would not be very simple if you then transitioned in the relief, but presumably over the transition period you may end up with the same level of forestalling; it is hard to tell. With any measure where there is a potential tax saving or a tax increase being introduced, there will be forestalling. Unless you can have it there and then—and clearly this needed systems to come into place to be able to implement it—it is very difficult, as Bill says; it is difficult to know how you would have zero forestalling.

Q205 **Mr Steve Baker:** Is there any particular advice you would offer the Government on when they ought to bring in a tax measure like this overnight and when they ought to defer it, consult and allow an element of forestalling?

Chas Roy-Chowdhury: The thing I do not understand about this policy is we have had the policy, which came in last year; it is going next year. It would be good if we stuck to the policy. In some ways you are going to get forestalling at both ends, so is that a good way of implementing tax policy? That is one piece of advice I would give.

Q206 **Mr Steve Baker:** On this measure of stability, has this particular policy fallen short of what is required to give us stability in the tax system? You are nodding but could you say “yes” for the record?

Nick Parker: Yes. Yes, the answer does have to be yes, and one does have to question the policy from the start, in that the goal of the Government was stop or to try to stop remuneration being diverted through dividends. That is quite rightly what the Government were trying to do. Whether in actual fact the introduction of the complex dividend allowance has achieved that is questionable. Would it have been better perhaps to limit it to dividends from unquoted companies? That would have been a much more targeted provision and perhaps would have avoided some of the unnecessary consequences that have flowed from it.

Q207 **Mr Steve Baker:** Mr Parker, that is a very good point, and you have just raised the next issue on my list, which is the complexity of the software in the tax system, something that I saw in my previous career. I can certainly attest to the complexity of tax software systems. Do you think there is a danger that, with the interaction of several related areas of tax policy here, people could end up paying the wrong tax because of excessive complexity in the software? You are all nodding, so I will get you all to put this on the record in the moment, but people end up paying the wrong tax through no fault of their own because the software is wrong.

Bill Dodwell: The Revenue has confirmed that.

Nick Parker: There are three instances—and there is an article that has been published, which I can circulate to the Committee afterwards so you have it on record—where HMRC has admitted that their software will get



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the tax wrong unless you submit your return via a paper tax return. That cannot be right.

Q208 **Mr Steve Baker:** Did they give any indication about whether they could or intended to fix it? Forgive me—I have not seen the article.

Nick Parker: They are trying to fix it, but certainly for the 2016-17 year, which is just about to be returned, they cannot fix it.

Bill Dodwell: They have said they will fix it for 2017-18, and the issues are the interaction between the allocation of the personal allowance across different sources of income taxed at different levels; the £0 to £5,000 exempt band of savings and income; the dividend allowance of £5,000 moving eventually to £2,000; and then the personal savings allowance of £1,000 or £500, and getting all those around has proved very hard.

Q209 **Mr Steve Baker:** Is it fair to say that the agility of tax policy is greater than the agility of the software development process? Is that what seems to have happened?

Bill Dodwell: I would argue that there are quite a lot of people who just do not understand how much tax they are due to pay and what the tax outcome might be if they invest it in a bank or they invest it in shares. For me that is a failure of tax policy, because the taxpayer ought to be able to understand the effect on their choices of the tax system. It is so complicated—and much of the blame obviously rests with the previous Chancellor, who introduced many of these things—few of us can understand it. Unless we have got really accurate software, it is really hard to calculate too.

Q210 **Mr Steve Baker:** Finally, just to draw some of this together, Mr Parker gave the indication that perhaps we should have just said it only applied to unquoted companies to try to deal with the perceived mischief of businesspeople incorporating for the purpose etc. Bearing in mind what we have just said about complexity, what advice would you give on having a more targeted measure? Do you think the Government should do it or not?

Nick Parker: I believe it should have been more targeted. Let me give you an example. If you had a pensioner who had £10,000 worth of pension income and £10,000 of dividend income pre this change, they were of no interest to HMRC at all because their pension income was covered by their personal allowance and their dividend income was already taxed: basic rate—no interest at all. With these changes, they end up with a £350 tax bill. Question mark: will the pensioner be aware that they now have to do a tax return? They were of no interest to HMRC before, so they may not be returning it, so they may be falling foul of the system. Secondly, they were not the target. That was not what the Government were trying to achieve. I would have thought it should have been much more targeted.



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Q211 **Mr Steve Baker:** I thought we had covered the ground extremely quickly there, but you have just raised another issue. You mentioned that they will get a £350 tax bill. Do you happen to know what the cost of recovering that £350 will be?

Nick Parker: No, I do not.

Chas Roy-Chowdhury: Also when might it be recovered, because who would know that that money was owed? The whole system now is such that, under self-assessment, the pensioner that Nick mentioned would probably never put their hand up. They would never know that they owed any tax, and HMRC themselves would probably never know either.

Q212 **Mr Steve Baker:** They would end up non-compliant through no fault of their own, and should the system catch up with them later, it will be at interest and they will be sent all sorts of hideous letters. Again, there is a degree of nodding. Could you just say “yes” for the record?

Chas Roy-Chowdhury: Yes.

Nick Parker: I agree with that.

Bill Dodwell: We are halfway through a system where the theory of the UK is that most of the work is done for you principally through the Pay As You Earn system, and it used to be on interest and dividends withholding, and then a minority of people had to do tax returns at the end. That is in contrast with the US, for example where everyone has to do a return. We are now, through the digitisation, going to try to deal with more of this through getting institutions to send in reports to the Revenue so that for all us, to the extent that we earn interest income, there will be better, more timely reports given, but the Revenue and the Government have not announced where this is going with other important items for the tax return. I would have thought it would be sensible for the Government and the Revenue to set out a plan so that we can all see when dividends perhaps go into this, when pension contributions go into this—another really important thing—and potentially even where higher amounts of charitable donations, Gift Aid, go in. After interest, those are the next three biggest categories of items that appear on tax returns.

We do not have a road map. We do not have something to enable people there to start gathering data to make sure it is you, Steve Baker, as opposed to a different Steve Baker, because obviously many of us have people with similar names, and try to get that spot on such that our tax can be corrected during the year. That requires a lot more effort than has been shown so far.

Q213 **Chair:** Given the complexity and certainly the controversy that may come with this measure, and given that we are now going to have a General Election, is this one that might best get dropped from this Finance Bill and parked so that it can be given some serious consideration? I am going to go from right to left this time: yes or no?



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Chas Roy-Chowdhury: Yes.

Nick Parker: Yes.

Bill Dodwell: No. It is simple to cut the rate of the allowance from £5,000 to £2,000.

Q214 **Chair:** We are just going to have yes or no to these questions, and I suspect we may be moving on to probate, which looks like a tax to me even though it is called a fee, and no doubt Jacob will ask you the same question on that.

Q215 **Mr Jacob Rees-Mogg:** Good morning, gentlemen. You have come in on a much more exciting morning than any of us had anticipated but, anyway, thank you for giving us your expertise. Indeed, I am coming on to the probate tax, which is thought to be classified by the Office for National Statistics as a tax and has been deemed a tax by the Joint Committee on Statutory Instruments. Do you agree that it is essentially a tax or do any of you think it is a legitimate fee?

Chas Roy-Chowdhury: I agree it is a tax. The increase is going to be a tax. Before it was a charge for undertaking that small amount of work that was required, but now, if it goes to £20,000, that is way beyond that cost.

Nick Parker: It clearly is a tax. It is not linked to the work that is being done and it was heralded in the original consultation document that it was there to contribute to the running of the court. An uncontentious probate never really goes near a court, so it is clearly a money-raising exercise.

Q216 **Mr Jacob Rees-Mogg:** As a money-raising exercise, is it not odd that it is reverting back to the slab system that was deemed to be so unfavourable in terms of stamp duty? Is there any reason any of the three of you can think of why it is worth going back to the slab system? I do not want to lead the witnesses, but it is quite difficult to avoid.

Bill Dodwell: The argument is it is relatively simple and the amounts involved are relatively small. I know when you hit an estate of £2 million, which of course is a tiny fraction of estates in England and Wales, it jumps to £20,000, but the vast majority are below a million and therefore the fee is not materially changed or is actually reduced for some.

Q217 **Chair:** It is similar to the inheritance tax surcharge, isn't it?

Bill Dodwell: I agree.

Q218 **Mr Jacob Rees-Mogg:** It is a slab inheritance tax.

Nick Parker: It perhaps would have been more sensible to have an ad valorem type: a fixed rate, at whatever percentage you want, on whatever size the estate is. That perhaps would have been better than slabs.



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Q219 Mr Jacob Rees-Mogg: But doesn't it have slightly perverse effects in that inheritance tax has a number of specific exemptions, which Parliament has brought in for good reason, none of which apply? There is a tax on widows; it is a tax on trading companies. All of this now gets caught.

Bill Dodwell: It is a tax on charities.

Q220 Mr Jacob Rees-Mogg: It is a tax on charitable giving. Do you think this is what was intended or are these the accidental consequences of something that was not necessarily particularly well thought through because it was not done by the Treasury?

Chas Roy-Chowdhury: That is exactly the point: the people who devised it did not really know about tax.

Q221 Mr Jacob Rees-Mogg: And so it is—the Ministry of Justice have come with it. Our clerks have come up with a brilliantly perverse consequence: on the death of a second married couple civil partner in May 2020, with an estate valued at £1 million and one penny, with the main residence left to the children, the inheritance tax charge would be £0.40 but the probate fee would be £8,000, and there may not be £8,000 of cash. This may be £1 million all in the family home, at which point the family home has to be sold to pay the tax, which was the whole point of taking the level up to £1 million in the first place. We seem to be getting to the point where another department has come up with a clever wheeze that is undermining a strand of a perhaps better thought through tax policy.

Bill Dodwell: If you have a million-pound house, you can probably raise £8,000 but, yes, it is a different policy.

Q222 Mr Jacob Rees-Mogg: Even in the current circumstances the banks might be able to lend £8,000 on £1 million of security. I wonder if you have any views constitutionally, because it is proposed to come through merely on a statutory instrument, on whether it is right that taxes should be able to avoid the full rigour of a Finance Bill and whether there is something wrong with that in principle.

Chas Roy-Chowdhury: Yes, there is, and I hope that with the election being called, those 776 pages do not just go through as they did in 2015 in two or three hours. There needs to be proper scrutiny by Parliament, rather than something going through by statutory instrument, when it comes to anything in the tax field.

Q223 Mr Jacob Rees-Mogg: Can we do the same as we did last time? Can I ask all three of you in turn whether you think this is something that in the washout period should be dropped?

Chas Roy-Chowdhury: Yes.

Nick Parker: Yes.

Bill Dodwell: Yes.



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Chair: Very clear, and since Jeremy Corbyn has said that he supports the Prime Minister's decision to put this before Parliament, it seems that the likelihood of it occurring has increased from high to almost certain.

Q224 Kit Malthouse: Can I declare interest as a member of the Institute of Chartered Accountants in England and Wales of some nearly three decades now? I wanted to ask you a little bit about Making Tax Digital, which is obviously in the Bill, but before I do that, related to Steve Baker's questions, do you think overall the Revenue benefits from the complexity of the system? Do you think the errors and mistakes are broadly in their favour or against?

Chas Roy-Chowdhury: The OBR response you had on MTD, which we have had shared with us—

Q225 Kit Malthouse: Not just on MTD but generally overall. You talked about this complexity foxing people—that the tax system has become a bit like that game with a ball and three cups, and you all take a guess about which cup your tax is under.

Bill Dodwell: I do not think the economy benefits from excessive complexity. We cannot simply go to a straight single flat-rate system, so we are bound to have some form of complexity, but excessive is just hard for the Revenue to understand; it is hard to programme; it is hard for business and individuals to understand; and everyone spends unnecessary resources in trying to deal with it.

Q226 Kit Malthouse: I guess the question I am asking is whether the Revenue has any incentive to simplify. Obviously their incentive is to collect as much tax as possible. If by injecting complexity into the system incrementally the tax just goes up and up and up, whether it is through error, whether it is through accident or design, and if they do it the other way—

Bill Dodwell: That sounds a bit Machiavellian to me. I am not sure I could take that.

Chas Roy-Chowdhury: I have always thought that the average taxpayer is not taking all the tax breaks they are entitled to; for example, we are entitled to take deductions for our professional fees as employees or you may find that you are entitled to some other deduction as an individual, and there are those kinds of errors, which are ongoing and they are very much in the Revenue's favour. Simplifying the tax system and the tax gap that the Revenue puts out every year does not adequately take account of the errors the individual makes in favour of the Exchequer.

Q227 Kit Malthouse: That is it, and the whole business case of Making Tax Digital is predicated on this notion that all the errors are in the businesses' favour and not in the Revenue's favour.



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Bill Dodwell: It is predicated on the basis the net error is in the businesses' favour and requiring people to keep records contemporaneously will reduce error, and that will boost tax, because they will record both receipts and expenses and, on the basis most people make a net profit—which they do—will just produce an overall tax—

Q228 **Kit Malthouse:** Yes, but, as I say, that is based on the assumption that the error is all in favour of business and that the net error is not the other way. The Treasury think they are going to collect over a billion quid or something extra off the back of this £1.3 billion in investment, and that seems to be what underpins the whole thing. I was just interested, because you said previously your view generally was that the error was the other way, and so we may well find that the Revenue loses money, not gains money, off Making Tax Digital.

Nevertheless, we saw some amendments in the Bill. Mr Parker, in the Autumn Statement, on your traffic light system I notice you gave red lights across the board on Making Tax Digital, and for the Budget you have gone to amber and green—I think one green and everything else is amber. Presumably, that is purely because of the extra year grace given to businesses under the VAT threshold.

Nick Parker: Yes, absolutely. We were very pleased that the Minister had listened, indeed to your Chairman and indeed to all of the institutes that had responded to them—just bringing in this £10,000 threshold was frankly ludicrous and there needed to be much more time. Talking to my counterpart at CIOT, he has just been to Australia, and the Australians are introducing a similar thing but they are doing it in a slower way. They are tiering it; they are bringing the larger businesses in first—a bit like Rti—to make sure that they get the system working right before the vast majority come in.

Q229 **Chair:** Could we have a note on that experience and the parallels and lessons to be drawn from it—preferably sooner than later?

Nick Parker: Yes.

Q230 **Chair:** There will not be much time. I am sorry to interrupt, but that would be useful to have on the record.

Nick Parker: Yes, I can ask. John Preston is the Deputy President of CIOT and he has just been there and spoke at a conference and met with some officials, so I am sure he can do something.

Chair: Thank you.

Q231 **Kit Malthouse:** Much of the correspondence that I got about Making Tax Digital in the run-up—and I guess I declare an interest as the owner of a small business as well that will be caught by this—was that there was a general objection to the principle of quarterly reporting. It was not necessarily an objection to reporting digitally but the principle of the



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frequency of reporting and that that would be an undue burden. I wondered from the movement in your traffic lights whether you had dropped that particular objection.

Nick Parker: No. We are still questioning why you do need to report on a quarterly basis. It is not particularly clear what HMRC are going to do with all of this information that they are getting, and I do not believe that it is improving the system. It is very high level at the moment, which is the issue, given that something is coming in in a year's time, particularly on how the software is going to work with regard to spreadsheets etc. because we know lots of business, quite rightly, do not keep their accounting records in accounting packages. They use spreadsheets, which is perfectly adequate, and how HMRC are going to link their software into random spreadsheets is highly questionable I would say.

Q232 **Kit Malthouse:** You still have practical objections to the implementation of the policy overall, notwithstanding the extra year's grace that has been given to some small businesses.

Nick Parker: We support the concept of Making Tax Digital, but it needs to be looked at in a much more pragmatic way in order to make it work. We are anxious that it works and that is the key point. I am not sure that it is necessarily going to work given the rush there seems to be of implementation.

Q233 **Kit Malthouse:** Right. On the current timetable, you would all still forecast some form of chaos when it comes in.

Bill Dodwell: That is more likely than not. As we understand it, there are 400,000 larger businesses—those above the VAT threshold. They already do quarterly reporting, because the VAT return is a quarterly report, so they do something. Many of those larger businesses will currently have accounting software, but there are lots and lots of different packages around and it is really uncertain today whether in one year's time, when this officially starts, all of the packages that these businesses use will have converted and will be able to make the reporting and all that sort of thing.

As Nick has just said, there is also absolutely no announcement regarding software that allows you to take a Making Tax Digital compliant spreadsheet and upload that into the Revenue system. That is why we all feel very uncertain: we have announcements but businesses want software that works, and we have not yet seen any sign of that. I have no doubt that all of the biggest software companies are working on it.

Q234 **Kit Malthouse:** This is the free software that is supposedly getting—

Bill Dodwell: That is a different point, because the free software is targeted really at those below the VAT threshold. It specifically will not do VAT calculations or is not required to do so, and so that is in 2019 rather than 2018. I am more concerned initially about more complicated accounting software that people use to run their businesses. There are



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supposedly many hundreds of different types. The reason there are so many is because there are so many different shapes of business and different industries. If you are a garage, you need entirely different software from a farm, for example, and it is that sort of complexity. We just do not know how it is going to work at this stage.

Nick Parker: Even a VAT-registered business does not need to have software. It can work perfectly well with a spreadsheet. My wife had a business, which she sold last year, that turned over about £140,000, and unsurprisingly I kept the books but it was done on spreadsheets, and it worked perfectly well; VAT returns were done—completely compliant. You did not need accounting software to run that business.

Chas Roy-Chowdhury: The thing I would add is that if businesses are going to be saving so much in administration, as the HMRC figures show, why do they need mandation? Why can the system not be voluntarily? That is the key part about MTD bringing in something through mandation. As Nick was saying, at the very small end, we have the £83,000 exemption for the first year, but it is targeted at those who are not as capable. If the business, rather than spending all of their time dealing with administration in doing five returns a year, sees it as a cost saving, they will come into it. I just do not see that it stacks up from HMRC's talk of cost savings for the business. It would not have to be made mandatory if that were the case.

Nick Parker: The point is also that people who have rental properties do not see themselves as "businesses".

Q235 **Kit Malthouse:** Notwithstanding this change in the Finance Bill, you still think more time is needed, possibly a voluntary basis and they should look at the Australian model. As you were saying, Mr Dodwell, you think there is effectively going to be a rush of botched software. You said earlier to Steve Baker that the software cannot work out the tax itself, so there are going to be all sorts of issues. In among all of that then—if there is a rush to compliance because business gets taken by surprise—there has been a big dispute between the Revenue and the FSB about the compliance cost overall. The Revenue has put out some figures saying it is going to cost business nothing—sort of 50 quid extra or something a year—and then you talk to businesses, who these days will not say anything to the Revenue unadvised, quarterly or otherwise. Where do you come down, you three, on the compliance cost?

Bill Dodwell: The Revenue's figures are done in aggregate. According to their letters, they expect that 60% of those below the VAT threshold will get free software, and so for them the costs are a bit of training and that is about it. We wonder how realistic it is that 60%—2 million people—will be able to have free software that maintains their accounts and does all their tax compliance for them. We think it is much more likely that that will end up becoming a fee-paying service, if not instantly at start; it will certainly migrate into that, and it will certainly be a form



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that will require that you move into that. We think 2 million people benefitting from free software is really quite unlikely.

Q236 **Chair:** What is the cost to business on average in that category?

Bill Dodwell: The cheapest package you are talking about is about £10 a month, so £120 a year, and then the question is: what about the training and do you need some advice in implementation? That is uncertain and will depend on the competence of the individual.

Q237 **Kit Malthouse:** Presumably if that is the case, Mr Parker, the Institute will be gearing up, because there is going to be a boom in advice required. Rather than once a year, it is four times a year.

Nick Parker: To some extent that has been the conflict that we have had, in that our members are, to some extent, sitting there rubbing their hands because they suddenly see this as a fantastic work stream. On the other hand, we have to defend the public interest, and is it in the public interest? But many of our members are actually saying that Making Tax Digital could be wonderful for us.

Q238 **Chair:** You do not think it is in the public interest but you do think it is in the interest of accountants?

Nick Parker: Correct.

Chas Roy-Chowdhury: I am not entirely sure. I do not disagree with Nick, but when we had a meeting with David Gauke in January of last year, when he was in charge of this area, the members with small practices we took along considered they could not charge any more to their clients, and they are the very low end—gardening and those kind of trades. When we had this discussion last year as well at the TC, we brought up hill farmers, for example. There is a real concern that a lot of small businesses will not be able to afford the fees. While it may be a business opportunity for some professional advisers, others will either have to swallow the fee increase or sack some of their clients, and some of the individuals and small businesses will perhaps become non-compliant through not being able to afford the advice.

Q239 **Kit Malthouse:** One of the examples, of course, which we would pray in aid, is the change in audit requirement, where despite the threshold being lifted for audit, you still see quite a lot of abbreviated accounts that do not require audit that come with an accountant certificate, because the business does not feel capable of putting them together themselves.

Q240 **Chair:** To be clear, this is a candidate for parking or for going ahead with. We do not want a long answer.

Bill Dodwell: A phasing.

Q241 **Chair:** There is no phasing in the current proposals, so you presumably want it parked and not to be part of the current Finance Bill?

Bill Dodwell: Yes.



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Nick Parker: Yes.

Chas Roy-Chowdhury: Yes.

Q242 **George Kerevan:** I want to move on and look at the Soft Drinks Industry Levy, which still does not come in until next year, but the Chancellor took the advantage of the March budget to add a few more tweaks. Are we any nearer to getting a clear definition in law between firms that are likely to be paying and those that are exempt, or will we end up in litigation?

Bill Dodwell: Firstly, I am not a soft drinks expert, it is fair to say. You will need to get some other people to help you with that. The briefing I have had says that it looks like we are getting closer to having an understanding of exactly what is in and what is not. You may argue about whether the boundary is being drawn rightly, because obviously some things that are not in have quite high levels of sugar, but the briefing I have got says we are closer to understanding who is liable.

Chas Roy-Chowdhury: Can I just widen this? I know it is something that we should not suggest, but it is hugely complex and, as you have said yourself, could be the subject of litigation if you are on the wrong side of the line. Why do we not look at some sort of duty against sugar? That is really what we are on about; we are saying that sugar is the bad thing that we are trying to reduce. Why do we not look at that rather than going round the houses? You are going to hit the same target. Yes, there may be instances where people who are less well-off and want sugar are going to be impacted, but there are substitutes for sugar. Maybe we need to look at the target we are trying to hit rather than going round all sorts of other things to try to hit that target.

Nick Parker: Are you suggesting something like tobacco?

Chas Roy-Chowdhury: Yes, at a very reduced level, and see how that works.

Q243 **George Kerevan:** A tax on the actual sugar content, rather than starting with the definition of the drink and working backwards.

Chas Roy-Chowdhury: Yes.

Q244 **George Kerevan:** That would be logical. The reason why I raised it was because I saw in the CIOT analysis of the budget changes that CIOT was querying the use of the word "beverage" in the actual legislation, because there is a track record in terms of litigation that might be triggered by the use of the that word specifically in the legislation.

Bill Dodwell: I suspect the tribunal will take the common sense view that a beverage is something you drink, and there you are—reach that conclusion.

Q245 **George Kerevan:** What really intrigued me about the Chancellor's Budget statement when he got to the Soft Drinks Industry Levy was his



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rather joyous statement that in fact the projected tax receipts were already falling because companies were reformulating the drinks. However, because it is a hypothecated tax, he was duty-bound to say that the expenditure that he had predicted would still go ahead. One just wonders whether that tells us anything about hypothecated taxes. Would anyone care to comment on that?

Bill Dodwell: We are not in favour of hypothecated taxes at all. We think taxes should be raised generally and spending should be dealt with separately.

Kit Malthouse: Nonsense.

Q246 **George Kerevan:** I think we have unanimity there. I agree. There is an argument for a sin tax on sugar, but the way it has been proposed is a bit of a mess. We will leave that and we will move on to another issue that I wanted to raise, which was the VAT Flat Rate Scheme that has come in, which I am already getting letters about in my constituency postbag. It has been brought in in order to deal with some anomalies in terms of employees being put on to self-employment off company rolls. In terms of the scheme as now being implemented, do you think it will effectively do away with some of the anomalies there were before in the flat-rate scheme?

Bill Dodwell: The idea of a flat-rate scheme is that it is simple to implement and those opting for it will almost certainly pay over less VAT than if they had done the proper accounting of VAT on purchases and VAT on sales and handed over the correct amount. It is a saving for the business involved, and the reason for the change is that the Revenue became aware that there was some quite significant abuse occurring, where businesses that did not qualify have been fragmented into lots of little micro businesses so as to benefit from this. The change they put is to essentially increase the flat rate for mainly labour-type businesses. That is the biggest change.

It is still possible to duck and weave around it for those minded to step around the clear intention of the law. That is not something we would advise people to do, but we cannot tell you it is bulletproof. But the end result has to be that maybe this is a simplification that people are taking advantage of in a manner that Parliament cannot really have intended, and unfortunately that is the challenge from it.

Nick Parker: But it is questionable, isn't it, whether this was the right way to do it and whether it is too complicated?

Q247 **George Kerevan:** Was there a better way of doing it—of removing anomalies?

Nick Parker: You could have just increased the rates, couldn't you?

Bill Dodwell: That is what has happened, fundamentally. The rate for labour only has been increased.



Nick Parker: But there is more complication there, isn't there?

Bill Dodwell: Yes, there is.

Q248 **George Kerevan:** What likely collateral damage might there be in terms of costs to businesses?

Bill Dodwell: I find it hard to think of collateral damage here. Yes, it is true that some businesses that were operating the system entirely honestly, entirely as Parliament intended, will now have to hand over more VAT, but we go back to the principal point: if they charge their customer 20% VAT, and they have got a limited amount of VAT paid out on their costs, they should have handed the net over. The flat-rate scheme meant they were paying over less than the normal amount, and now they are going to pay a bit more but still less than the normal amount.

Q249 **George Kerevan:** But in the processing, are there likely to be any administrative costs that will add to the burden on small businesses?

Bill Dodwell: No, because unless you are trying to duck and weave, anti-avoidance will not apply; the rate has simply changed.

Chair: Thank you very much for coming to give evidence on this somewhat more eventful day than we had bargained for. I think we are clear that you think the key measures that we came here to discuss should be put into cold storage for a while at the very least. For the record, everyone is nodding their head in agreement, which tells us something about what we think about the quality of the measures. Thank you very much for coming to give evidence. The Committee will meet tomorrow to take decisions on what further scrutiny it might try to conduct on what will inevitably be a dramatically truncated Budget, and there is one piece of written evidence that we are very grateful to all three of you for agreeing to supply to us. Thank you for coming.