The complexity of simplification

General Features



29 September 2020

Bill Dodwell reviews the issues faced by the Office of Tax Simplification and its efforts to address complexity in tax

One of the seemingly perennial questions concerns what exactly the Office of Tax Simplification is supposed to do. What is simplification? The OTS was given statutory authority in 2016, by virtue of the Finance Act 2016 Sch 25 and ss 184-190. The Act has this to say (s 185):

1. The OTS must provide advice to the Chancellor of the Exchequer, on request or as the OTS considers appropriate, on the simplification of the tax system.

2. For the purposes of this section and s 186:
   (a) ‘the tax system’ means the law relating to, and the administration of, relevant taxes;
   (b) ‘relevant taxes’ means taxes that the Commissioners for Her Majesty’s Revenue and Customs are responsible for collecting and managing; and
   (c) a reference to ‘taxes’ includes a reference to duties and national insurance contributions.
3. References in this section and s 186 (however expressed) to the simplification of the tax system include references to improving the efficiency of the administration of relevant taxes.

The Act thus doesn’t define simplification, other than making it clear that it includes improving the efficiency of administration. We therefore need to consider the ordinary meaning of the word.

What does it all mean?

The Cambridge Dictionary defines simplification as ‘the process of making something less complicated and therefore easier to do or understand’.

Sir Edward Troup, speaking in February 2019, suggested that simplification relates particularly to certainty, the burden of undertaking tax compliance, and the tax system’s comprehensibility (see bit.ly/3hutlyt). He pointed out that the OTS’s work has at times involved suggesting reforms where it can especially have a role in preparing the ground, seeking to revise how the system operates. Optimistically, Troup also saw the OTS as acting as a restraint on the government through its wider influence.

Administrative improvements and beyond

Possibly the greatest part of OTS reports is focused on administrative improvements; and in recent years, due to the pressure on parliamentary time, it has been important to work on these matters. Good examples here include the 2018 report on HMRC Guidance and the first inheritance tax report, which focused on improving the administration of the tax. The current study on claims and elections will doubtless include many suggestions for improvement.

Simplification must go further than administrative improvements if it is to be truly successful, however. It was striking to find from the inheritance tax survey,

completed by over 3,000 people, how little was understood about the tax by potential taxpayers. Some of the recommendations for inheritance tax policy change are designed to make the scheme of the tax easier to follow – by those without tax expertise.

Changes to achieve this ambition have been criticised by some experts, but surely remain at the heart of the Office's mission. The chief focus of the Office is on benefiting the majority of taxpayers, with particular (but not exclusive) consideration given to those without ready access to tax advice. Having an understandable framework is a simplification, even if there are some complexities in the law.

The complexity of choice

Choice is in many ways a good thing. However, in taxation too much choice, or unhelpful choice, adds complexity. An individual wishing to be self-employed can provide services directly or can exercise choice to establish a company to provide those services. The taxation consequences are quite different – and complicated.

The OTS heard in its 'Simplifying everyday tax for smaller businesses' report that many people ended up with a company, which they didn't understand (see bit.ly/2FzFpkO). Individuals didn't realise that a company is a legal person separate from its owners and directors. Evidence shows that the overwhelming majority of small (micro) companies have a tax agent, almost certainly because the owners don't understand how to manage a company. Yet 30% of self-employed individuals manage their accounting and tax affairs without help.

We cannot (and should not) remove from people the choice of legal form but providing more help and support to those starting up on their own could help. Others have argued that looking in more depth at the neutrality of the overall tax system would make it easier for choice to be based primarily on business reasons, rather than for tax reasons.

A further area of complexity is created by distortions in the tax system. There are numerous examples where different tax treatments encourage people to do something in a particular way to achieve a tax advantage. If the distortions were reduced, people would act in a simpler way. One example concerns gifts of chargeable assets by a parent to children. Often the capital gains tax advice will be to hold on to the asset, to benefit from the market value step-up on death; yet the better approach, from a business or family perspective, might be to pass on the

asset much sooner.

Stimulating consideration

One of the challenges for the UK tax system generally is how best to stimulate consideration of possible changes.

After all, general consent is an important part of the effectiveness of any tax system. I would argue that in some areas the Office of Tax Simplification is best placed to lead this broader review of future options. The Office has done work of this sort in the past; for example, with its exploration of a common base for income tax and national insurance.

A more recent example is the scoping report on Reporting and Paying Tax, which looked at the case and opportunities to extend third party reporting to help self-employed individuals and landlords with their tax compliance obligations (see bit.ly/3mpZVFm). The review suggested that there are some parts of the economy where this type of reporting is possible and would be helpful.

The Financial Secretary to the Treasury Jesse Norman MP, speaking the recent Tenth Anniversary OTS conference, welcomed that the OTS ‘has been prepared to have that engaged, intelligent, expert conversation with government that allows it to address policies that affect large numbers of taxpayers’. He also strongly reaffirmed his support for simplification of the tax system – both as an end in itself and as a way to reduce costs for taxpayers and for HMRC. (The conference recording is available at bit.ly/35TiDzt.)

Ultimately, the work undertaken by the OTS depends to a great part on what interests the chancellor, HM Treasury or HMRC – since they have the decision-making power. The independence and the unusual public sector/private sector mix of the OTS means that it is well placed to research and recommend substantive improvements to the UK tax system.