



ICAEW REPRESENTATION 161/16

TAX REPRESENTATION

Public confidence in HMRC's capability to collect tax fairly and effectively Inquiry of the All Party Parliamentary Group (APPG) Responsible Tax

ICAEW welcomes the opportunity to comment on the [Inquiry into public confidence in HMRC's capability to collect tax fairly and effectively](#) by the All Party Parliamentary Group (APPG) - Responsible Tax which opened formally on 8 September 2016.

This response of 28 October 2016 has been prepared on behalf of ICAEW by the Tax Faculty. Internationally recognised as a source of expertise, the Faculty is a leading authority on taxation. It is responsible for making submissions to tax authorities on behalf of ICAEW and does this with support from over 130 volunteers, many of whom are well-known names in the tax world. Appendix 1 sets out the ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark proposals for changes to the tax system.

We should be happy to discuss any aspect of our comments and to take part in any future Hearings on this topic.

Contents

Paragraphs

General comments	1 - 24
Responses to specific questions	25 - 52
Ten Tenets for a Better Tax System	Appendix 1

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GENERAL COMMENTS

Some initial, background, remarks

1. We believe that it will be helpful to set out some general remarks about tax systems and how they are operated in developed countries and the UK in particular.

The international dimension

2. There has been a lot of dissatisfaction expressed over recent years about the way in which tax systems work and in the outcomes of such systems.
3. The UK has played a key role in taking steps to address the deficiencies in the existing international tax arrangements. During its presidency of the G8, now G7, in 2013 a number of key issues were identified at the June 2013 G20 Summit at Loch Erne and positive steps were put in train to address them. This led to the G20/OECD work on Base Erosion Profit Shifting (BEPS) and to subsequent work on country by country reporting, automatic exchange of information and work to provide information about the beneficial ownership of entities.
4. On the first of those action points OECD and G20 have worked on BEPS (Base Erosion Profit Shifting), to recalibrate the international tax system and to make domestic tax systems operate more coherently with each other.
5. BEPS was the subject of the first APPG Responsible Tax Inquiry to which ICAEW submitted a response and Ian Young, Technical Tax Manager, gave oral evidence to the Inquiry in March 2016. .
6. At the more micro level it is important that those involved in tax systems have an appropriate relationship to make sure the tax systems, and tax rules, work – and are perceived by all stakeholders as working - in the way that was intended.
7. In a ground breaking study carried out in 2006-08 into the role of tax Intermediaries (more commonly referred to as tax advisers) OECD reached the conclusion that a well-functioning tax system requires a robust and constructive engagement between tax administrations, taxpayers and tax advisers. This has been taken forward by OECD in a more general work stream under the current title of “Cooperative Compliance”.
8. This has been the modus operandi in the UK of the HMRC Large Business Directorate within which there is a CRM (Customer Relationship Manager) for each of the more than 2,000 large businesses dealt with by the Large Business Directorate. The CRM is responsible for handling the HMRC relationship with the particular business to ensure that HMRC understands how the business operates and can take a knowledgeable, but robust, attitude to the tax implications of the commercial activities of the particular business. This way of working helps to prevent differences of opinion escalating into disputes which are extremely resource intensive for both taxpayer and HMRC.
9. Since the publication of the OECD report in January 2008, and the subsequent financial recession in 2007-08, there has been a much greater interest from society more generally into the proper functioning of tax systems. We believe that public interest is absolutely appropriate and that concerns of the wider public into the workings and outcomes of tax systems need to be addressed.

The UK and HMRC

10. In terms of the UK tax system a very large percentage of the money which HMRC collects comes in as a consequence of the system itself, for example through PAYE for employment taxes and National Insurance Contributions and through collection of VAT by business. The three major UK taxes (income tax, NIC and VAT) account for 75 % of the total UK tax take according to the HMRC Annual Report and Accounts 2015-16. The UK system is founded on a very high level of voluntary compliance.

11. There has been an increasing concern over the past 10 years about tax avoidance and preventing tax evasion. HMRC has published an annual report on [Measuring Tax Gaps from 2009 onwards](#). It has published details of VAT tax gap in technical papers alongside each year's Pre Budget Report beginning in 2001. An annual technical paper assesses the value of the Measuring Tax Gaps papers and the most recent was published in October 2015 [Background quality report: measuring tax gaps](#). The most recent estimate of the Tax Gap was published in October 2016 [Measuring Tax Gaps 2016 edition](#).
12. Over recent years HMRC has been criticised by the press, Parliamentary committees and the public for failing to tackle large businesses over perceived aggressive/unacceptable tax avoidance and for poor service delivery. The criticisms of HMRC in respect of the former have reflected the international public mood on the issue.
13. Criticisms of service delivery began to surface shortly after the creation of HMRC from its predecessor departments, H M Customs & Excise and the Inland Revenue. There have been particular criticisms of call centre performance, post handling and the adequacy of the increasingly impersonal interface between HMRC and taxpayers. There is also a perception (fairly or unfairly) that big businesses receive better – and fairer - treatment than smaller businesses.
14. HMRC's headcount has reduced substantially since its creation and many – including ICAEW - have seen this and the fall in service standards as a matter of cause and effect. This is an issue we have expressed concern over on many occasions. The loss of personnel has not just affected response times but arguably also the quality of response, as many of HMRC's most experienced people have been lost.
15. In recent years ICAEW Tax Faculty has commissioned annual reports into HMRC Customer Service Standards and the results of the most recent survey were published in January 2016 [TAXREP 1/16 HMRC Customer Service Standards 2015](#)

The Digital Dimension

16. HMRC has (in common with many other tax authorities) made significant moves to digital channels for taxpayer contact. Making Tax Digital (MTD) is about to create the biggest change in tax administration in a generation. While HMRC has some real successes to celebrate in the migration to digital compliance, there is evidence to suggest that it is not taking on board all of the lessons learned from previous digital initiatives. One lesson to be learned is that headcount should not be reduced simply in anticipation of efficiency saving through digital channels, but only when those efficiencies have actually been realised.
17. Considerable use has also been made by HMRC of technology and digital tools to target enquiry resource more effectively.
18. We are fully supportive of the use of digital technology to modernise and improve tax compliance but believe that HMRC does not always fully understand the impact of such moves on taxpayers (whether individuals or businesses) or draw all necessary lessons from past experience. HMRC accepts for example that some changes – such as the use of iXBRL (tagging of business accounts), RTI (Real Time Information for PAYE) and now MTD – will give rise to transitional or “one-off” costs but is reluctant to acknowledge the imposition of additional ongoing costs. Many businesses have shouldered additional ongoing cost burdens as a result and MTD is likely to lead to even more as businesses are compelled by HMRC to maintain their records digitally.
19. For example, the changes proposed by the Making Tax Digital consultations, are as much about simplifying and cost-cutting for HMRC, and gathering more information about taxpayers, at the expense of the taxpayer. Making Tax Digital would be more accurately described as Making Business Digital as it will require all but the smallest businesses to keep their accounting records using an App on a smartphone or software on a computer. Excel

spreadsheets are not currently going to be acceptable for this although very many businesses use them.

20. The target commencement dates seem overly optimistic for what is undoubtedly a significant change for taxpayers and HMRC alike, especially bearing in mind past problems with IT related change experienced by HMRC and other Government Departments. In collecting evidence for HMRC's RTI post implementation review which recently closed, we received many complaints from our members who act for large numbers of payrolls that differences between HMRC's figures and their own remain unreconciled. In most instances, the agent knows their figures are correct, but HMRC seem unable to amend their own records to reflect these. This does not bode well for the proposed MTD launch date of April 2018.
21. The change seems likely to add to the compliance costs borne by most taxpayers. Whilst it may be the case that efficiency gains can be made by tax accounting on a real time, or close to real time, basis, it seems doubtful that these gains for taxpayers will be that significant, compared to the time spent already in compiling information when returns are due. It seems probable that the overwhelming majority of taxpayers will have to invest in acquiring software, apps and, perhaps, hardware (computers, tablets and/or smartphones) to enable compliance with their new obligations to interface with HMRC systems at least quarter

Other comments

22. HMRC has gone through several changes of governance structure since its formation and a period of structural stability would be helpful.
23. Over recent years HMRC has acquired a formidable array of powers. This adds to the importance of HMRC ensuring that the public regard the use of powers as fair and proportionate.
24. In the context of the above general remarks we have included, below, specific comments in response to the more detailed questions:

RESPONSES TO SPECIFIC QUESTIONS

Q1: What levels of trust and confidence do the public have in the capability of HMRC to collect tax in an effective way that:

- a) preserves and encourages fairness and equity?
- b) is an efficient and effective use of resources?
- c) provides a first rate customer service

25. HMRC has been under considerable scrutiny in recent years and has come in for considerable criticism, not least from the Public Accounts Committee.
26. HMRC has been undertaking a very considerable transformation of the way in which it operates and this will continue for the foreseeable future, not least as a result of the Making Tax Digital project. This has been coupled with a more centralised approach and a considerable reduction in numbers of staff (see our response to question 3).
27. The criticism of HMRC has led to a feeling in the public domain that the UK tax system is not as fair and as equitable as it could be. That perception is perhaps as much a product of the design of the tax system itself as of the way in which the tax system is administered by HMRC.

Q2: What can be done to improve the levels of public confidence in HMRC's capability?

28. There needs to be a well-informed, robust and public debate about the tax system, HMRC's role and how the tax system is performing by reference to its many different tasks.

29. HMRC should certainly articulate its successes when things are going well, but be prepared to acknowledge honestly when things are not going as well as they should (and be clear about what the department is doing to correct the latter). For instance call centre response times went seriously awry in 2015 (see our answer to question 3), but instead of acknowledging the problem HMRC stopped publishing quarterly statistics until they had improved while responding to questions by simply saying that current response times were under five minutes. Transparency is vital to building trust.
30. HMRC also needs to tackle head-on the often expressed perception in the small business community that large business gets a better deal. Forcing small businesses to adopt digital record keeping is unlikely to help change the feeling of unfairness.
31. We believe that the core issues are resources and public perception.
32. We will follow with interest the work that HMRC and the NAO is embarking on to establish whether there is a link between service delivery and attitudes to tax compliance. The UK tax system operates as well as it does because of the extremely high level of voluntary compliance and we believe that this should not be taken for granted: confidence must be maintained.

Customer service:

Q3: Does HMRC provide a first rate customer service?

33. The government has cut the head count in HMRC very significantly over recent years.
34. The HMRC Development Plan 2014 – 16 shows, in the chart on page 16, that the HMRC headcount dropped from just over 91,000 in 2005 to just over 61,000 in 2014.
35. In recent years this drop in headcount has been accompanied by a drop in customer service, particularly in the early part of 2015 which was highlighted in the National Audit Office (NAO) report of May 2016. [The quality of service for personal taxpayers.](#)
36. Over the last year the HMRC level of customer service has improved in some areas (for example call centres), but this is in part because more resource has been allocated to these areas and because of initiatives such as “once and done” which empowers staff to resolve issues quickly. This improvement is also in part down to better use of technology. We fear that when headcount is reduced again service standards will fall once again.

Q4: To what extent does HMRC consider the customer's experience in the allocation of its resources and the services it provides?

37. HMRC aims to put the customer at the heart of everything that it does, but that is not always how it is perceived or experienced by the customer.
38. We believe the new enhanced status of Your Charter within HMRC (the Charter Committee is now one of only four direct Sub-Committees of the HMRC Board), provides HMRC with a chance to better realise its ambitions to treat the customer as being at the heart of all it does – and perhaps more importantly, as being seen to do so.
39. We would particularly commend the value of spending more time with individuals and small businesses to understand their issues and to see the tax system through their eyes. When HMRC does this it achieves better results in terms of customer-centric delivery.

Q5: Is the HMRC strategy for improving the customer experience fit for purpose?

40. We would encourage HMRC to listen to its customers and to engage with them openly in order to understand their perceptions of the tax system and administration and particularly to understand how small businesses operate.

Dealing with tax avoidance and evasion:

Q6: How effective is HMRC in dealing with

a) aggressive tax avoidance?

b) tax evasion?

Aggressive tax avoidance

41. A considerable number of new legislative powers have been introduced in the past couple of years to combat what HMRC and government describe as aggressive tax avoidance. It is too early to determine how successful these new measures will be or how effective HMRC is in using them.
42. In recent years the Government has introduced measures against the Promoters of Tax Avoidance Schemes (POTAS), Accelerated Payment Notices (APNs) and Follower Notices in addition to a General Anti-Abuse Rule (GAAR), introduced in 2013.
43. The conclusions and recommendations from the April 2016 NAO report Tackling tax fraud, quoted below, set out clear recommendations for HMRC to improve the quality of its reports on the risks that it faces in administering the tax system and how well it is addressing them.
44. We believe that resource and experience is again an issue here.

Tax evasion

45. Both the NAO and the PAC have published reports within the past 12 months on the HMRC work to cut back on tax fraud [Tackling tax fraud: how HMRC responds to tax evasion, the hidden economy and criminal attacks \(NAO\)](#) published in December 2015 and [Tackling tax fraud: how HMRC responds to tax evasion, the hidden economy and criminal attacks](#) (PAC) published in April 2016.
46. The five detailed conclusions and recommendations in the April 2016 PAC report are:

“Tax compliance yield and the tax gap

PAC thinks there needs to be much greater clarity about the extra yield from tax compliance which is going up all the time, according to HMRC, while the tax gap remains stubbornly at the same level in money terms. HMRC should “publish the relationship between its compliance yields and changes in the tax gap in a way that is accessible for everyone to understand”

The strategy to tackle tax fraud

PAC wants this to be much more clearly articulated and asks for this to be done by November 2016. HMRC should identify how much resource is devoted to tackling different tax risks and the corresponding yield in each area of the tax gap.

HMRC needs to tackle the perception that it is not tough enough on tax fraud by the wealthy

PAC is concerned that only one HSBC client exposed in the Falciani list has been prosecuted and by HMRC's lack of data on wealthy individuals that have been prosecuted in recent years. The PAC recommendation is:

“HMRC must do more to tackle tax fraud and counter the belief that people are getting away with tax evasion. It needs to increase the number of investigations and prosecutions, including wealthy tax evaders, and publicise this work to deter others from evading tax and to send out a message that those who try will not get away with it.”

HMRC had a target of 1,000 additional prosecutions by 2014/15, which it met, but it is not clear what this has achieved

PAC thought that HMRC had probably met its target of a 1,000 increase in prosecutions by concentrating on simpler cases. It recommended that HMRC "should evaluate and quantify the impact of prosecutions and other counter-measures in deterring evasion".

HMRC has been slow to respond to the growing risk of VAT fraud by internet Traders

The PAC in the previous Parliament had taken evidence on this problem three times in 2013 but HMRC had presented in its January 2016 evidence session as if this was a new problem. New powers have subsequently been announced in the March 2016 Budget so the current PAC would like HMRC to review the previous PAC findings, identify the size of VAT internet fraud and let the current PAC know within the next 12 months how successful the 2016 Budget measures have been in tackling the problem."

Q7: What legislative, resourcing or other measures would help to narrow the tax gap?

47. We believe that the new measures that have been introduced over the past few years need to be given time to determine how successful they are in dealing with the behaviours which give rise to the tax gap.
48. There is a case for looking at the "informal" economy and at the understatement of income. We do not believe that Making Tax Digital will make any inroad into this problem.

Q8: Does HMRC make appropriate use of all the powers and opportunities in its toolkit?

49. It is arguable that better use could be made of HMRC's existing powers if it had more resource.

Staffing and resources:

Q9: Are HMRC's resources adequate?

50. In our view, no.

Q10: Is HMRC able to recruit and retain people with appropriate skills, qualifications and experience?

51. We are concerned that so many experienced and technically able people have been lost over recent years. We welcome HMRC's commitment to increase training activity and we believe that significant investment in training is vital. It is difficult for HMRC to compete in the marketplace but in the past it has managed to recruit people of high calibre and we see no reason why it should not be able to continue to do so.

Q11: Within constrained budgets, what could HMRC do to achieve better and more sustainable services?

52. It is clearly going to be beneficial for HMRC to make the tax system more digital and improve the efficiency and effectiveness of the system. There is a major consultation, ending in November, on Making Tax Digital and while we have significant concerns about some of the proposals we do believe that an increasingly digital approach to the tax system is the right way forward. We do not however think that HMRC should be forcing small businesses to take on a greater administrative burden simply to help HMRC: adoption should be a matter of choice and if digital really holds benefits for small business as HMRC claims, they will transition to digital voluntarily.

APPENDIX 1

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

The tax system should be:

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

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see via <http://www.icaew.com/en/about-icaew/what-we-do/technical-releases/tax>).