



ICAEW REPRESENTATION 16/17

TAX REPRESENTATION

OPTIONAL REMUNERATION ARRANGEMENTS (INCLUDING SALARY SACRIFICE)

DRAFT FINANCE BILL 2017 LEGISLATION: CLAUSE 2 & SCHEDULE 2

ICAEW welcomes the opportunity to comment on the [draft Finance Bill 2017 legislation](#) published by HMRC on 5 December 2016.

This response of 1 February 2017 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 all further consultations on this area.

On 5 January 2017 we attended a meeting with HMRC jointly with other professional bodies in which we were able to put forward some key comments and concerns and discuss aspects of the draft legislation. We also attended a joint bodies' meeting with HMRC on 5 September 2016 to discuss the Summer consultation proposals, to which we responded in [ICAEW REP 156/16](#).

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ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.

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OUR CONCERNS - SUMMARY

1. The commencement date needs to be put back to 6 April 2018 to give time for employers, HMRC and software houses to get ready and for software to be tested. In particular, HMRC needs to provide detailed IT specifications to the software community in line with the 18 month “Carter” protocol and redesign its forms, eg the 2017/18 P11D to capture “amounts foregone” and P46(Car)
2. Employers need to be made aware of the changes – a major publicity campaign is needed to alert employers and highlight which remuneration practices will be caught and what employers need to do under the new regime
3. “Arrangements” – clarification is needed about what this covers and Variation of contract – clarity is required about what this means
4. Private use contributions by employees and “modified cash equivalent” – clarification is needed about what this covers
5. Approved mileage allowance payments (AMAPs) need to be excluded from the rules (as stated to us by HMRC on 5 September 2016)
6. Provision of and transfer of assets – clarification is needed about the new rules
7. School fees – need to be excluded from the rules
8. Exemption for death or retirement provision – needs to be retained in line with the government’s commitment on pension provision
9. Employer-provided accommodation – the impact of the provision needs clarifying
10. Alternative to benefit of car or van offered – the impact of the provision needs clarifying
11. Exemption for workplace parking – needs to be retained
12. NIC – draft legislation needed and confirmation that commencement date will be the same as for tax

GENERAL COMMENTS

1. THE MEASURE

Our concern

As noted in our response to the summer consultation ([ICAEW REP 156/16](#) – see also our [newsitem](#)), the proposals run contrary to several of our *Ten Tenets for a Better Tax System* published in 1999 and summarized in Appendix 1, notably being neither simple, easy to collect and calculate, nor properly targeted, nor constant, nor subject to proper consultation nor competitive (these are similar to the principles for tax policy established by the Treasury Committee in its report of 15 March 2011).

The meetings with HMRC were welcome and constructive but too late in the consultative process.

What has become apparent following these meetings is that the draft legislation:

- contains a number of provisions that were included in error,

- will lead to some unintended consequences (for example, certain “lifestyle changes” being caught as a variation), and
- may lead to unfair outcomes (such as double taxation on the transfer of assets previously used by an employee).

Our recommendation

We urge the government to provide a detailed policy objective for the proposed changes so that consideration can be given to whether a sweeping change with many exceptions – many of which appear to be intended to be only in guidance – is the best method of achieving that objective or whether a targeted approach would better meet that objective.

We recommend that, as a matter of course, policy be worked up by way of draft guidance which is consulted upon to find out whether it is likely to work in practice before law is drafted. This would help to ensure that policies work in practice, and that policy, legislation and guidance align with one another and comply with our Ten Tenets and the Treasury Committee’s principles of tax policy.

2. CONSULTATION TIMING

Our concern

As noted above, we welcome the opportunity to help make the legislation better, but being asked to do this during the period leading up to the self assessment deadline means that many of our members who normally contribute to our representations are otherwise engaged in ensuring that their clients’ tax returns are submitted on time and therefore they are unable to spend time on non-remunerated work.

Our recommendation

We suggest that personal including employment taxes consultations that extend over the 31 January self assessment deadline have response deadlines set in mid-February at the earliest, rather than, as in this case, 1 February.

SPECIFIC COMMENTS

1. COMMENCEMENT DATE

The measure

The new rules are scheduled to take effect from 6 April 2017. Those already in salary sacrifice contracts at that date will become subject to the new rules in respect of those contracts at the earlier of:

- an end, change, modification or renewal of the contract, and
- 6 April 2018, except for cars, accommodation and school fees when the last date is 6 April 2021.

Our concern

Despite the government extending the grandfathering period to the dates noted above, which we welcome, employers will be unable to comply with all the new requirements by the start date of 6 April 2017 because there are too many uncertainties, including:

- The proposed law is convoluted and unclear (eg the meaning of “arrangements”, the date that arrangements are made which are or are not within the provisions, employees making good – see below for these and other examples) and will not be final until Finance Act 2017 receives Royal Assent, probably in July 2017, over three months after the measure comes into effect.
- HMRC will be unable to finalise its guidance until after Royal Assent in July 2017 notwithstanding the government’s undertaking that “*The government will ensure that*

guidance is prepared in readiness for this change". HMRC is still drafting guidance on payrolling of BiK and changes to the expenses rules from April 2016.

- Information technology (IT) software designers need eighteen months to design, build, test and install software for calculating the BiK for human resources (HR) and payrolling, and train operators. With only two months until "go-live" we are not aware that HMRC has even issued preliminary IT specifications. The principles laid down by Lord Carter in his 2006 report [Review of HMRC Online Services](#) have been ignored. We would note here that presently the quantum of cash foregone is not needed for P11D reporting purposes so will be a new field for IT developers of P11D software.
- HR departments will need to devise new remuneration structures and processes and revise internal guidance.
- Employers will need to renegotiate contracts with employees and suppliers of BiK.
- Many employers are not aware that they will be affected.
- HMRC has announced that it is not amending its form P46(car) until April 2018.

Our recommendation

We consider that the commencement date should be put back to 6 April 2018 and 2021 as appropriate.

This would not only give time for HMRC to:

- provide detailed IT specifications to the software community in line with the 18 month "Carter" protocol, and
- redesign the 2017/18 P11D to capture "amounts foregone" and form P46(Car),

but would also:

- enable employers, payroll bureaux, software houses and HMRC to prepare and test the IT to make sure it works properly (including HMRC being able to process the data accurately) and
- simplify the transition by doing away with the need to grandfather certain contracts until 2018 or 2021.

Suggested amendments

In para 21, in all places substitute "2018" for "2017" and substitute "2018-19" for "2017-18".

2. MAKING EMPLOYERS AWARE

Our concern

We believe that many employers are unaware not only of the imminent commencement of these provisions and that their remuneration practices will be caught by them, particularly where employers refer to their remuneration practices by names other than "optional remuneration arrangements" or "salary sacrifice", but also of what they should do to comply.

On awareness, some employers offer employers "cash allowances", eg a remuneration package of £30,000 plus a car allowance of £5,000 which can be taken in cash or as a company car. Other employers have "choice BIK" or "flex ben" schemes. Yet others allow employees to draw on pools of BiK. They may not realise which schemes are within the new rules.

We note that HMRC has published an article in *Employer Bulletin* (EB) under the title "salary sacrifice". However, many employers looking at the contents page will have assumed from the title that this article was not applicable to them so have not read it. We would also mention that we understand that EB is read by only a minority of employers.

Our recommendation

We recommend that HMRC carries out a major publicity programme in the national press, trade journals and online aimed at payrollers and their advisers, BiK providers and customers and human resources departments (ie much wider than the normal readership of *Employer Bulletin*) to ensure that all appropriate stakeholders are fully aware of whether and if so how these provisions

will affect them and what they will need to do, and in particular to make employers aware of the diversity of remuneration practices that will be caught by these provisions.

As part of an awareness campaign, detailed guidance will be needed on:

- what types of arrangements are covered, highlighting that the provisions are not restricted to “salary sacrifice”;
- the effect of pre-contractual discussions and at what point an employee will be considered entitled to earnings which are an alternative to a benefit,
- if the start date is not put back, variations of a contract from the point of grandfathering, highlighting when a variation is acceptable because it is under a contract compared with a variation outside of the contract, and
- when under a flexible benefit scheme an extra family member being added to insurance etc. is a variation or considered a separate new arrangement so the conditions that HMRC would impose to ensure that any grandfathering is not lost.

See also the other topics below, all of which should be explained in clear and concise legislation but we fear are likely to be need to be explained in guidance given the complexity and opaqueness of the proposed legislation.

Suggested amendment

In the title of new s69A after “Optional remuneration” insert “and flexible benefits”.

3 “ARRANGEMENTS” (para 1 (new s69A) & para 25 of Sch 2) and VARIATIONS OF CONTRACTS

Our concern

The meaning of “arrangements” and when a contract is considered to have been varied are unclear.

Our recommendations

We should welcome clarification in the legislation of “arrangements” and at what point contracts are considered to have been varied, in particular:

- What employees and employers need to have done by 5 April 2017 (or a revised start date) to be a “pre-6 April 2017 arrangement” in para 25(2);
- Confirmation that the new provisions apply only when and where the employee has the option to choose or whether they apply when the employer can choose. Whether a change such as adding or removing a family member to or from a contract, eg medical insurance constitutes a variation under para 25(7); and
- Whether the new provisions apply if:
 - the employee exchanges one BiK for another, or
 - a flexible benefit scheme respectively does and does not include a cash allowance.

On the first bullet, we should welcome confirmation that if, by way of example, employees are required to notify by, say, 21 February 2017 via their employer’s online flexi-benefits system which BiK they wish to have in exchange for cash earnings for the tax year 2017/18, this is without doubt a “pre-6 April 2017 arrangement”.

4. PRIVATE USE CONTRIBUTIONS BY EMPLOYEES & “MODIFIED CASH EQUIVALENT”

Our concern

The draft legislation does not appear to provide for employees to be able to extinguish the taxable value of the BiK by making good to their employer an amount equal to the value chargeable to tax and NIC, or to reduce it by paying a lesser amount. We believe that it should.

The legislation provides that the calculation of each specific BIK is amended so that there is a “modified cash equivalent” which is compared with the cash foregone to give the relevant amount. It would have been simpler if there was one overriding “modified” cash equivalent when the amount foregone is more than the “standard cash equivalent” of the benefit

On the basis of the draft legislation, if an individual makes a contribution towards the provision of certain assets, for example a van, as well as the sacrificing cash it appears that the amount contributed will not reduce the “relevant amount”, even though the contribution is after all being made from after-tax and NIC income.

Our recommendation

We should welcome confirmation that the legislation will provide that employees can extinguish or reduce the amounts chargeable to tax and NIC under the new provisions and will explain clearly how to calculate how much employees need to pay their employer to extinguish the BiK charge, ie whether the value of the BiK calculated using normal rules or by reference to the amount of cash earnings foregone.

5. APPROVED MILEAGE ALLOWANCE PAYMENTS (AMAPS)

Our concern

At the meeting with HMRC on 5 September 2016 to discuss the summer consultation document we were assured that AMAPs would be excluded from the new provisions. However the draft legislation does affect them so an exclusion needs to be inserted.

To explain, at present, where AMAPS are not paid in full (ie 45p per mile for the first 10,000 business miles and 25p thereafter for tax and 45p per mile for NIC purposes), employees can claim tax relief (on form P87 if not in self assessment) for the difference between the 45p/25p per mile allowed and the amount recovered from their employer. We see no mischief in letting employees choose between receiving for example either:

- i) a monthly cash allowance (liable to tax and NIC) plus 45p/25p per business mile, or
- ii) a higher monthly cash allowance and a smaller per business mile mileage payment, at say AFR rates, with the employee making a claim (eg on form P87) to recover the tax on the difference between 45p/25p per mile and the mileage rate paid by the employer, or
- iii) a monthly cash business mileage allowance plus a smaller per business mileage payment with the employer dealing with the tax and NIC via the payroll.

Where employees have to make claims on form P87 it means significant extra work for employees in completing those forms and HMRC in having to review and process those claims. To obviate this, some employers offer salary exchanges to employees who drive business miles in their own cars, and account for the tax and NIC via the payroll, as in iii) above. For example, an employer gives its employees £500 business miles allowance per month and pays business mileage of 12p per business mile. If the employee drives no business miles in that month, the employer pays the employee the full £500 subject to deducting tax and Class 1 NIC. If the employee drives business miles in their own car, the employer pays the employee 12p per mile (perhaps via payroll as an addition to net pay) and in the payroll does not deduct tax or NIC on a further 33p/13p per mile which is deducted from the £500 car allowance, so the employee currently receives the full 45p/25p per business mile tax free and 45ppm NIC free as provided for in current legislation.

However, under the new provisions, because the 33p/13p was exchanged for what would have been cash earnings, it appears that the employee will be taxed and subject to NIC on the 33p/13p foregone. This is despite the employee having driven their own car and therefore being entitled to 45p/25p tax free and 45p NIC free. On first impression it might appear that the employee could submit a form P87 to recover tax relief on the 33p/13p taxed via payroll, but the employee will be barred from doing this because under s231 ITEPA such claims are supposed to be based on the

difference between the full AMAP amount, namely 45p/25p, and the amount that the employee was paid by his employer, ie 45p/25p.

We see this as being the loss of a genuine relief, and unfair on those employees who are paid the 45ppm in conjunction with a salary exchange. Such staff will suffer a tax charge on a legitimate business expense with no possibility of claiming relief as they have received the full 45p from their employer.

Our recommendation

We should welcome confirmation that where the exchange of an allowance for a business mileage reimbursement occurs because the employee has driven and claimed from his employer reimbursement for business miles under AMAP, the new provisions are not intended to apply.

For the avoidance of doubt, the legislation needs to confirm that AMAPs are exempted from the new rules

Suggested amendments

In para 21, either define “benefit” in new 69A(4) to exclude cash business expenses or exclude business mileage payments made at, or below, AMAP rates as defined in s229 and s230 ITEPA, and, in para 21, in new s228A(5) include s229 approved mileage payments as a further “excluded exemption”.

6. PROVISION OF AND TRANSFER OF ASSETS

Our concern

If an employee is provided with an asset such as a fridge worth £600 and after three years the asset is transferred to the employee, then the current rules are that the employee is charged a cash equivalent of 20% of the market value, ie £120 per year cash equivalent (s205 ITEPA 2003). At the end of three years when the asset is transferred to the employee, the charge is the remaining 40% of the initial market value, ie initial market value less amounts previously charged at 20% per year (s206), ie £600 less (£120 x 3 = £360) which equals £240. In other words the employee is eventually charged on full market value of asset.

Under the current proposed legislation the employee would get charged on the amount sacrificed each year, say £200 per year. In total this would be £600 at the end of three years. When the asset is transferred to the employee, the employee would then be taxed on the same basis as above, meaning that £240 is taxed under the optional remuneration rules and again on s206, as it is not being amended to take account of the optional remuneration charge..

It appears unreasonable to us that the employee is charged tax twice under the proposal.

Our recommendation

We believe that s206 should be amended to allow for amounts charged as optional remuneration.

7. SCHOOL FEES

Our concern

We welcome in principle the attempt to mitigate the impact by grandfathering to 2021 but would note that as school fees contracts normally vary each academic year, because fees normally increase, the grandfathering will be of no effect, meaning that most of the children involved, for the greater part sons and daughters of teachers, are likely to have to change schools at the start of academic year 2017/18. It is also unfair to penalise younger siblings who miss the grandfathering cut-off date.

In addition, the wording at draft paragraph 25(11) of Schedule 2 will not cover situations where there is neither a payment nor a reimbursement, as the school makes no charge.

Our recommendation

We suggest that either school fees be excluded or grandfathering be extended to the child's 19th birthday and not be overruled by contract changes or variations, including changes of schools.

In addition, paragraph 25(11) should be amended to cover arrangements where fees are neither paid nor reimbursed.

8. EXEMPTION FOR DEATH OR RETIREMENT PROVISION (para 21)

Our concern

We believe that group income protection policies and excepted life policies should not be caught by the new rules. This is because, for example, if the group income protection policies are caught a double charge will arise in the premiums paid and on any payments under the policy. Currently the premiums are not a taxable BiK but the payments to the individual under such a policy are taxable. There would also be unequal treatment under salary sacrifice arrangements between death in service benefits under a registered pension scheme (s308) and other arrangements (s307) that give the same economic result.

Our recommendation

If employees are to be taxed on the provision of the insurance under the new provisions, then they should not be taxed on the receipt of any pay-out towards their salary.

We should welcome confirmation that the exemption in s307 ITEPA 2003 (death or retirement provision) in new section 228A(5)(e) (para 21 of Sch 2) will be retained under the provisions as an "excluded exemption" in line with the government's commitment to pension saving.

9. EMPLOYER-PROVIDED ACCOMMODATION (para 7)

Our concern

The cash equivalent under new s103A of living accommodation costing no more than £75,000 is simply the rental value (with no further legislative explanation). This differs from the current position under s105. Similarly, there will be no account taken of excess rent under current s106 for living accommodation costing more than £75,000.

Our recommendation

We should welcome confirmation that the changes in new s103A to s105 and s106 ITEPA have effect only in the context of these provisions and that the existing s105 and s106 will in cases where there is no salary sacrifice continue to apply as now.

This is an example of where having multiple versions of the same section will make the law unnecessarily confusing.

10. ALTERNATIVE TO BENEFIT OF CAR OR VAN OFFERED (para 8)

Our concerns

The amendments to s119 seem to lose the original policy intent of the forerunner to s119, which was to ensure that an employee is taxed on the car or van BiK where a trivial cash alternative is offered (in the absence of s119, tax and NIC would be charged on the cash alternative only).

We would mention that the changes to s119 remove all references to vans from the body of the section but retain the word "van" in the heading.

Our recommendations

We recommend that the original policy intent of s119 be reinstated and should welcome clarification of what the section is intended to achieve.

We suggest that the title and body of s119 be made consistent.

11. WORKPLACE PARKING

Our concern

The provision, by an employer to an employee, of “workplace parking” (as defined by s237(3) ITEPA 2003) at or near the employee’s workplace is exempt from both income tax and NIC (the NIC provisions are included within reg. 25 and paragraph V and paragraph 8 of part VIII of Schedule 3 to the Social Security (Contributions) Regulations 2001).

It is a long established principle, accepted by HMRC, that employees may enter into a legitimate salary sacrifice arrangements with their employer in order to cover the costs of workplace parking. The provision of workplace parking has previously been treated akin to that of employer provided childcare, cycles/equipment and pension contributions. When HMRC issued “full guidance on salary sacrifice” the related ‘Salary sacrifice Q&A’ also included confirmation that employees should be able to opt in and out of four exempt benefits, stating:

“Special legislation has been enacted to prevent this [the application of Heaton v Bell causing the salary sacrifice to fail] happening for the following exempt benefits:

- *Employer provided childcare*
- *Workplace parking*
- *Employer provided cycles and cycle safety equipment*
- *Employer made contributions under a registered pension scheme”*

This is confirmed at [EIM42755](#).

However, the proposed draft legislation appears to fundamentally alter the treatment as it relates to the provision of workplace parking.

We are unaware of any mischief, or potential avoidance concerns, where taxpayers have sought to manipulate the current provisions. In the case of workplace parking, employees have little choice in whether or not to incur additional costs relating to parking at their workplace. The impact of the current proposals is that many employees and employers will face a financial penalty from April 2017.

Reimbursement of workplace parking levy charges

Closely linked to the provision of workplace parking are situations where employers have been forced to pass on the incremental costs of providing workplace parking spaces to employees as a result of the implementation of the Workplace Parking Levy (WPL).

To explain, under the Transport Act 2000, local authorities in England and Wales (outside of London) were given powers to introduce a WPL to help tackle congestion in towns and cities. To date, the only local authority to have implemented a scheme is Nottingham City Council who introduced their scheme in April 2012. In Nottingham, employers who provide 10 or more car parking spaces to employees at or near their workplace are charged £375 per parking space per annum. The majority of employers have been forced to pass on this incremental costs associated with the provision of workplace parking to their employees. In fact, in many cases, employers had previously provided employees with free workplace parking.

When Nottingham’s WPL was introduced, as part of the implementation process, it was agreed that any employer who was passing on the costs to their employees would be allowed to offer this

via salary sacrifice. Again, a result of the draft proposed legislation is that there will be a significant number of employees within the Nottingham area who are detrimentally impacted.

We see this as being the loss of a genuine relief, and unfair on those employees who are impacted.

Our recommendation

We should welcome confirmation that the new provisions are not intended to apply to the provision by an employer to an employee of workplace parking.

For the avoidance of doubt, the legislation needs to confirm that arrangements relating to the provision of workplace parking are exempted from the new rules.

Suggested amendments

In para 21, define “benefit” in new 69A(4) to exclude the provision of workplace parking as defined by s237 ITEPA, and, in para 21, in new s228A(5) include s237 workplace parking as a further “excluded exemption”.

12. NATIONAL INSURANCE CONTRIBUTIONS

Introduction

We note that apart from cash vouchers there should in theory be no changes to NIC regulations as all that is changing or meant to change is the P11D value of a benefit, received in connection with an optional remuneration arrangement, and the Class 1A NIC simply applies to a different figure. Consequently, there should be no changes to primary or secondary NICs – apart from cash vouchers.

Our concern

Any changes to the NIC rules should start at the same time as the income tax provisions. Not doing so would be illogical and such inconsistencies bring the tax/NIC system into disrepute.

Our recommendation

We should welcome confirmation that any necessary changes to NIC will start at the same time as the tax changes and clarification of when the draft NIC regulations, and guidance if the regulations are not self-explanatory, will be published.

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>).