



Tax Faculty

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KEY ISSUES FOR THE 2006 PRE-BUDGET REPORT

*Text of a memorandum submitted in October 2006 by the
Institute of Chartered Accountants in England and Wales
to the Chancellor of the Exchequer*

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KEY ISSUES FOR THE 2006 PRE-BUDGET REPORT

ABOUT THE ICAEW

The role of chartered accountants in the world's economies has never been more important. People making financial decisions need knowledge and guidance based on the highest technical and ethical standards. Our members provide this better than anyone. They challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity.

As their Institute, we create this environment in which those skills are constantly developed, recognised and valued. We shape opinion, understanding and delivery, to ensure the highest standards in business and in the public interest.

Because of us, people can do business with confidence.

ABOUT THE ICAEW TAX FACULTY

The Institute's Tax Faculty speaks on behalf of the Institute on tax and Budget matters, drawing upon the expertise of members in business as well as the tax profession. It is concerned with the practical implications of taxation, including the impact on business and the economy, as well as the principles of good tax law.

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PART A - ENTERPRISE POLICY

Government's enterprise policy is evolving on a number of fronts. From regulation to business support to the Lyons review, the Institute appreciates that Government is exploring how it can better remove barriers to business and better encourage economic growth. The Institute, here, lays out a number of steps that together would help to reinvigorate enterprise policy and in turn help Government to better support the enterprise economy.

TACKLING THE COST OF NEW REGULATION

The Institute has welcomed the Government's Better Regulation Agenda, including the estimation of the administrative cost by departments of existing regulation, the setting of targets to reduce that cost and the Hampton review. The Institute also supported the Legislative and Regulatory Reform Bill as it will better allow Government to improve existing legislation. This is a sizeable and challenging programme for Government and the Institute will continue to play a constructive role.

However the Institute finds that the flux of new regulation remains largely unabated. The Institute's 2006 Enterprise Survey found that the cost of new regulation upon business is estimated at £7.7 billion, up from £6.9 billion last year. 74% of that impact is shown to fall on businesses with less than 10 employees. We believe that improving the process for new regulation so that it is better regulation, that costs business less and particularly costs small business less, is a priority. New regulation distracts entrepreneurs' attention away from doing business. Existing regulation, though also sometimes troubling, is often dealt with through well developed coping strategies.

Policy Recommendations

In order to improve new regulation, nothing less than a change in the UK's regulatory culture is needed. This requires a number of coordinated steps.

- The Better Regulation Executive's current proposals to improve RIAs, should be implemented as a significant improvement to the rigour, usefulness and practice of impact assessment.
- The Cabinet Office should now consult as a priority on improving Government's engagement with stakeholders throughout the regulatory process. Ensuring availability of expertise on small business impact within Government is another essential element to achieving cultural change.
- On RIA Summary Sheets, the proportion of impact on small business should be made transparently clear. The Small Firms Impact Test should then be dropped.
- Cabinet Office should develop a clearer, simpler and more transparent framework for how impact assessments should work which moves away from the previous box ticking approach.
- Maximising benefits and minimising costs should become the clear objective of all impact assessments rather than simply proving that benefits are greater than costs.

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PUTTING SMALL BUSINESS CONSIDERATIONS AT THE HEART OF GOVERNMENT

Small businesses are a major generator of growth in the UK. In the 2006 ICAEW Enterprise Survey, over 20% of micro and small companies are planning annual growth of over 30%, compared to only 4% of very large companies. Their flexibility and disproportionate ability to innovate are keys to the UK's future competitive standing in an increasingly global marketplace. The Institute therefore fully supports the importance placed on enterprise by HM Treasury. Yet even though over 99% of businesses are small, Government still too often thinks 'large business first.'

The already mentioned regressive cost of regulation on small business is a signal that Government's policy and actions are not always in harmony. The 2006 National Audit Office (NAO) Report into the Small Business Service demonstrated that Government, across the board, needs a better appreciation of its impacts on small business if it is to meet its objectives. The debate so far has focussed on reforming the Small Business Service. The Institute believes this step alone would at best skirt around the key problems and at worst delay real progress on this issue for years.

Policy Recommendations

For Government to take forward its enterprise policy, it now needs to ensure small business concerns are at the heart of all relevant policy making.

- HM Treasury should ensure that every Government Department has experienced Small Business Champions with the capability and experience to help the Department take full account of its impact on the enterprise economy.
- Small Business Champions would help those at the heart of policy making to identify and improve the impact of their proposed measures on small business - a more effective method than sending decisions, effectively already made, across to the SBS for a 'Small Firms Impact Test'.
- The SBS or a successor body should then come under the auspices of HM Treasury.
- The successor to the SBS should help maintain expertise across Government, working as an advisor to RDAs and local Government, managing specific small business policy and ensuring that simplicity in business support is maintained.
- The NAO should be tasked with performing regular external evaluation of pan-Government performance in dealing with small business interests.

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FOCUSING AND IMPROVING PUBLICLY FUNDED BUSINESS SUPPORT

The Institute supports the Government's objective to simplify and improve publicly funded business support, announced by the Chancellor in the March 2006 Budget. The practicality of achieving this across Departments and local government is a major challenge involving a number of critical policy choices.

The forthcoming Lyons Review could potentially threaten the Chancellor's objectives by resulting in more public bodies seeking the attention of SMEs for their own schemes. The Institute believes that it makes sense to devolve more responsibility for economic development to cities and localities. However, it is essential to provide simple and easy access for SMEs to available support.

Policy Recommendations

The Institute believes Government should look to better focus expenditure, improve the delivery and quality of schemes and develop systems for continual improvement.

- Publicly funded business support should be limited to providing help to business that the private sector does not on its own already provide – tackling the economic definition of market failure.
- Government support should act strategically to encourage market-led solutions to apparent market failure. Investment should then move on to other priorities.
- HM Treasury should make these policies clear in the forthcoming Budget and Comprehensive Spending Review.
- To meet the Chancellor's target, the DTI should develop a simple framework of a maximum 100 types of support scheme any part or level of government can provide.
- Central Government should cut to zero, or an absolute minimum, the economic development objectives it imposes on RDAs/local Government leaving them free to prioritise, innovate and choose between the 100 schemes.
- Utilising the private sector and business bodies should be the default option for delivering support to SMEs. Where this is not possible, RDA-Business Links should be the single gateway for support, even if funded by local Government.
- Business advice support should be provided by a voucher scheme that entrepreneurs in the driving seat can choose for themselves across the maximum choice of private sector providers.
- Evaluation and review should be integral to all business support service no matter who funds them or undertakes provision. Successful schemes should be replicated; poor schemes should be improved or removed.

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PART B - KEY TAX ISSUES

The Institute is keen to continue to work with HM Treasury and HMRC on the areas that we have identified to help improve the tax system and welcomes continued discussion of these vital topics.

We set out here a programme to improve the UK tax system which we believe would be of benefit to all its stakeholders. Tackling tax complexity, both in the rules and in the way they operate, is a key priority. This complexity creates uncertainty, increases administrative costs and undermines trust. In addition, steps need to be taken to address some of the other causes of the ‘trust gap’ that we believe has developed between HMRC and tax advisers and taxpayers. We appreciate many of our points have been mentioned before but believe that increasingly evidence from business is demonstrating their continued relevance. We also propose a number of further measures to combat criminal fraud in the VAT system.

The Tax Faculty has identified ten key principles (the Ten Tenets) that should underpin a good tax system. We use these to benchmark the tax system and they are set out in Annex A.

IMPROVING THE UK’S TAX RULES

A recent press release by the tax publishers Butterworths Lexis Nexis confirmed what many tax advisers already knew; namely that the amount of UK tax legislation has doubled within the past ten years. Whilst we appreciate that Government is engaged in a programme of tax reform in and has adopted a robust approach to tackling tax avoidance, we now have a hugely complicated tax system that is caught in a culture of constant change. Much of the newer legislation is unclear and often too widely targeted. We would welcome a move towards providing a clear purposive statement before legislation is implemented setting out its aim or the real ‘mischief’ it is targeting. We believe this will reduce some of the confusion that can arise when complex measures are introduced.

In order for a system of self assessment to succeed we must tackle the issue of complexity. Simpler tax law engenders respect from taxpayers and encourages compliance. We also suspect that many HMRC staff are also struggling to cope with the demands being placed upon them by the never-ending changes and continued increased complexity. For ordinary taxpayers doing anything other than minimum economic activity, they have little chance of understanding their way around the tax system without the help of an agent or adviser.

Such a highly complicated and impenetrable tax system is not in the interests of UK plc and we consider that something should be done to redress the balance. Many of our recommendations below are not new; we and others have been saying them now for some years. However, we think that the time has come for a bold approach from Government to take on board these measures. We believe there is a desire from all

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sides to have clear, properly targeted legislation and as we approach the next Finance Bill cycle it is an ideal opportunity to reverse the trend of recent years.

Policy recommendations

The problem of tax complexity is deep rooted and the causes are many. We believe firmly that the solutions lie in a shared understanding of the issues and problems, coupled with a will from all stakeholders in the tax system to bring about long term improvements. We think that the time has now come for more concerted action. Particular areas that need to be addressed are set out below:

A long-term programme to simplify the tax system - We have made repeated calls of the need to simplify the tax system. We are pleased that this key message appears to be widely supported by others, including Government. The Tax Law Rewrite Project has now been in place for over ten years (it was originally proposed to be a five-year project). The work of the Tax Law Rewrite team has been valuable but, after ten years, we believe that their work has highlighted that much more radical action is needed if the UK tax system is to be made fit for the 21st century.

Improving the legislative process - High quality tax legislation depends upon informed and detailed Parliamentary scrutiny. We appreciate that the time for considering Finance Bills is extremely limited, but we think several improvements could be made to the process which will help to improve the quality of tax legislation. The annual Finance Bill process means that, broadly, UK plc only has 'one shot' to hit the target. It is all too easy to miss the target first time around and, whilst of course mistakes are corrected and further refinements made at a later date, this process is highly unsatisfactory for all concerned and often creates considerable uncertainty in the meantime. Time should be taken at the beginning to try and ensure that tax legislation is 'right first time' rather than iteratively, only arriving at a satisfactory solution after many years. The process could be improved by adopting some or all of the measures set out below.

- i. Separating revenue-raising Finance Bills from technical Tax Bills should be considered. The latter types of Bill should not be tied so closely to the Budget cycle and more time than at present should be allowed to ensure that the legislation is 'fit for purpose', ie the legislation not only puts into effect what is intended but also can be applied in practice without difficulty. This will allow more time to be invested by stakeholders, such as ourselves, to ensure that the legislation achieves what it is meant to achieve.

Adopting such a 'two track' process would then enable officials of Government Departments to provide oral briefings and explanations as the Bills pass through Parliaments. Furthermore, we think that Government needs to be more innovative in seeking the views of stakeholders when tax rules are being formulated. For example, it should be possible for the committee charged with scrutinising a technical tax Bill to call on tax experts to help inform their work so that, whilst working within the overall policy framework set by the Government, new UK tax legislation is fit for purpose when it is enacted. It may also be possible to draw on the considerable experience in these matters of certain members of the House of

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Lords (subject of course to respecting the overriding authority on these matters of the House of Commons).

- ii. Purposive legislation may be one way to reduce the volume and complexity of UK tax legislation. Decisions of the Courts appear to be focusing increasingly on ‘the purpose’ behind the legislation. This may be an opportune time to consider further with stakeholders, the advantages and disadvantages of adopting a purposive approach to legislation.
- iii. In the meantime, we believe Government should set out the policy objective of tax legislation either by way of a Ministerial statement in the House, or preferably by way of a statement in the HM Treasury Finance Bill Notes on Clauses, published at the same time as the Finance Bill.

IMPROVING TAXPAYER SERVICES

All stakeholders in the UK tax system have a shared interest in suggesting and making improvements. This is recognised by Government; and HMRC is refocussing to be an ‘enabling organisation’. One of HMRC’s three key objectives is to ‘improve the customer experience – support businesses and reduce the compliance burden.’. We welcome the commitment to these objectives and will work with HMRC to help build a tax system that is fit for the 21st century.

We are, however, concerned that HMRC is being starved of both the resources and time needed to translate this strategic objective into reality. The words and the vision need to be supported with the necessary resources to invest in change and bring about improvements within a realistic timetable, as otherwise the vision is unlikely to be realised. Our concerns, based upon the practical experience of our members, are that far from taxpayers’ experiences improving, they are at best static and in some areas declining, as evidenced by the examples below.

Delivery of electronic services - The 2004/05 employer end-of-year filing system was not ready when it went live in 2005, and the validation system had to be disabled to enable e-filers to use it. Even today in October 2006, some 2004/05 end-of-year returns and incentive payments still have not been processed, although we appreciate that HMRC have now said that these will be brought up to date and paid by the end of this month.

Restructuring of HMRC - The continuing restructuring of HMRC, with the consequent closure of local offices, the redeployment of staff elsewhere and an increased reliance on call centres as the key customer contact point, appears to be causing considerable damage to the operation of the tax system on the ground. The local liaison between the tax authority and taxpayers and agents provided a common meeting point and an ability to get to understand local issues. The loss of this structure has led to a reduction in regular contact and potentially of mutual understanding. HMRC is of course required to reduce its staff numbers over the next few years by over 10,000 and this is likely to exacerbate what is already a growing problem.

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Whilst we recognise that the UK needs a highly streamlined and competitive tax administration, we are concerned that these developments are a case of ‘too much, too soon’, not least because technological developments have yet to make a real impact in improving services to taxpayers. The changes appear to have resulted in a loss of both local and specific case knowledge, the cost of which cannot readily be translated into monetary value but in terms of staff efficiency – and morale – must be considerable. We believe that the experience of customers has deteriorated, and this is leading to considerable frustration for taxpayers and their agents.

VAT registration - The increasing delays suffered by taxpayers registering for VAT are causing us great concern. HMRC should not cause business to suffer damaging delays of weeks or months when they wish to start trading. We appreciate that new controls have been introduced to counter MTIC fraud, but that is only part of the cause. In any event, this is an example of inadequate staff resource allocation within HMRC.

Policy recommendation

- i. HMRC and its customers should reconsider how HMRC services its customers and how the existing levels of service can be improved. Whilst returning to the former ‘District’ structure may no longer be possible, we think that practical steps could be taken to improve local dialogue and accountability, for example by nominated staff ‘owning’ particular issues and by the nomination of named staff as a contact point for tax agents.

WORKING WITH AGENTS, CONSULTATION AND TRANSPARENCY

There is a widespread recognition across the spectrum that there is a real need to rebuild trust and confidence between the tax authorities and taxpayers, their agents and advisers.

A ‘trust gap’ has opened up between the tax authorities on the one hand and taxpayers and their agents and advisers on the other hand. Many of the issues that have given rise to the trust gap were highlighted in the roadshows that the Tax Faculty undertook with senior members of HMRC around the country in 2006.

A combination of factors over a considerable period of time are to blame. Once lost, trust is hard to regain. Action now needs to be taken to close the gap and considerable patience and commitment will be required from all sides to do so.

At the operational level, we think that tax accountants and agents, employers and taxpayers generally perceive that the level of service provided by HMRC has declined (see our earlier comments above) and that too often the standard of service is poor. At the strategic level, there is widespread dismay that the consultation process has been undermined by poorly thought out policy changes introduced with little or no warning and then compounded by an apparent unwillingness to work collaboratively with the professions to improve the policy announcement so as to make them workable before

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the legislation is enacted. Examples include the Pre-Owned Asset regime introduced in 2005 and the IHT changes for trusts in the Finance Act 2006.

Partly in response to this 'trust gap', HMRC has established a new 'Agents and Advisers' Team and we have participated actively in its first few meetings. We welcome that development but think that much more needs to be done to close the 'trust gap'.

Policy recommendation

- i. We believe that the Agents and Advisers Team should have as an overriding objective the task of working with tax agents and advisers to reduce, and in time eliminate, the 'trust gap'. Both sides need to work together if this gap is to be reduced and we are considering further the ways in which the professions might work more closely with HMRC to increase confidence and understanding. In order to move this forward, we would like to work more closely with HMRC and share with them our more detailed thoughts on how the 'trust gap' can be bridged.

HMRC POWERS AND MANAGEMENT ACT REVIEWS

We welcome the various reviews of HMRC powers (including the updating of the Taxes Management Act) and believe there is a real opportunity to modernise the rules and make them more effective and fair for all. We remain concerned that HMRC have been tasked with conducting this review, rather than an independent body, since this will inevitably be seen as prejudicing the outcome. We are also concerned that there will be insufficient time for proper public consultation and consideration before legislation is enacted. The risk is that the outcome will not achieve a proper balance between the rights and safeguards for the citizen and the additional powers and penalties given to the tax authorities.

The merger of the former HM Customs & Excise and Inland Revenue provides an obvious springboard for considering whether the existing powers, rights, safeguards and obligations inherited by HMRC are appropriate to a tax authority operating in the 21st century and whether they can be rationalised across the new Department. However, we do have several concerns, not least that the emphasis appears to be more on making changes quickly than considering whether changes are needed.

We are concerned that the rush to legislate is not providing sufficient time to review the issues. For example, the interventions pilot which began in July 2006 has highlighted how a project which should point to improvements in the system can falter on an operational level when it is rushed, lacking in adequate technical back-up material and forced out in timescales that cannot be achieved. There are important lessons to learn from this project which will help ensure that future suggested plans do not run into the same difficulties. The alternative is that the 'trust gap' we have referred to earlier will increase further.

In addition, we understand that it is proposed that the Joint Parliamentary Committee procedure that is used for Tax Law Rewrite Acts will be used to enact the New

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Management Act. This is a special procedure for what is in reality non-contentious legislation. We do not think that this special procedure is the appropriate mechanism for proper scrutiny of a new Management Act, which appears likely to make significant changes to the legislation. The contentious issues should be resolved beforehand in accordance with the usual procedures and there should be full consultation on the underlying policy and wording of the new Management Bill in an open and collaborative manner.

Policy recommendations

- i. We consider that such a fundamental review as HMRC powers should be carried out in a coordinated manner over a timescale appropriate to what is a substantial task and engage the professional experts in a way which enables them to contribute in a more positive way.
- ii. We are concerned that significant proposals will be put forward for inclusion in the Finance Bill 2007 without adequate time for full consideration. We believe that any firm proposals should be given adequate time for consultation and that full and open consultation should be sought within, as a minimum, the consultation timescales set out in the Code of Practice on consultations produced by the Cabinet Office.

IMPROVING THE E-BUSINESS EXPERIENCE

The Institute fully supports the Government's desire to encourage the use of e-services. It is critical to the success of HMRC's e-services that the 'e-experience' offered by HMRC compares favourably with that offered in the private sector, for example on-line banking. Lord Carter's report made a number of key recommendations so as to ensure that HMRC's electronic services are robust, reliable, user friendly and can cope with capacity peaks.

For those at the sharp end of dealing with HMRC electronically, whether in business or in practice or, indeed, as private individuals, probably the most important of Lord Carter's recommendations are that:

- 'HMRC should benchmark customer satisfaction with its online services against commercial online services and seek to learn from best practice.' (Recommendation 2); and
- 'as part of their work to deliver robust, high-capacity services HMRC should build in more rigorous testing. Each of the services should be capacity tested at least a year before our recommendations are implemented, and if any tests are not successful the measures relating to that service should be deferred.' (Recommendation 23).

We recognise that HMRC is making considerable progress in developing its electronic services in line with these recommendations. Nevertheless there is still a long way to go to achieve high levels of customer satisfaction. We believe that the principles set

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out in recommendation 23 – we have called them the ‘Carter Principle’ - are fundamental to the success of HMRC’s e-services.

Policy recommendation

- i. It is essential that proper testing of all systems is undertaken in line with the Carter Principle. Electronic services should not be introduced (and certainly not made compulsory) if the Carter Principles are not met in full. We are liaising closely with HMRC via various consultative committees and we are doing all we can to help ensure that the e-business experience that HMRC offer their customers is fit for the 21st century.

MONEY LAUNDERING AND COMPLIANCE MONITORING BY HMRC

An HM Treasury consultation paper issued on 31 July 2006 on the implementation of the 3rd Money Laundering Directive (see http://www.hm-treasury.gov.uk/consultations_and_legislation/money_laundering_directive/consult_thirdmoney_index.cfm) proposes that HMRC should take on responsibility for monitoring compliance with anti-money laundering rules by, inter alia, auditors, external accountants, tax advisers and those who provide company and trustee services who are not members of designated bodies.

We do not think that HMRC should undertake this work. At a practical level, we do not think that HMRC has the resources to cope with its existing functions, let alone making improvements to the customer experience. Over the past few years, HMRC’s duties have expanded over and above its core work of the collection of tax and management of the tax system, for example with the addition of tax credits. With the proposed reductions in HMRC’s resources, we doubt that HMRC have sufficient capacity to carry out the monitoring role proposed by HM Treasury.

More seriously, we believe that such a monitoring role is wrong in principle, due to a potential conflict of interest on the part of HMRC. We do not see how HMRC can combine its role of managing the tax system and dealing with taxpayers and their agents with a completely different role monitoring money laundering compliance over the same agents. The potential conflicts of interest make such a proposal a non-starter. We note that HM Treasury cite a precedent for this proposal, namely HM Customs & Excise’s monitoring role over money service businesses. However, given the merger between HM Customs & Excise and the Inland Revenue, we do not think that this is any longer a suitable precedent and it should not be followed. Indeed, we think that even this monitoring work should be removed to an independent monitoring unit.

Policy recommendations

- i. We recommend that the Office of Fair Trading be made responsible for anti-money laundering compliance monitoring, as suggested in the consultation document for estate agents, or the FSA.

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MISSING TRADER INTRA-COMMUNITY FRAUD

Missing Trader Intra-Community Fraud (MTIC) is clearly the most serious criminal attack on the VAT system since its introduction in 1973. The opportunity for MTIC fraud arises as there is no VAT on intra-Community transactions between taxable persons. We accept that estimates are difficult to make, although the latest unofficial estimate for the current year is some £8 billion, with the official (HMRC) estimate due to be announced in the Pre-Budget Report. We welcome recent press reports of a significant number of arrests of alleged perpetrators.

We have been pleased to work with HMRC in their campaign warning businesses of the danger signs (so that they do not inadvertently become involved with the fraud) and have highlighted this aspect in our communications with our members.

We have also welcomed the proposed introduction of the reverse charge for certain goods, although we see this very much as a temporary ameliorating measure rather than a cure. Our concern, of course, is that the fraud will probably switch to other goods and services not covered by the reverse charge provisions.

We have been critical of the actions taken by HMRC to counter MTIC fraud where they penalise the innocent rather than the guilty. Not only is such conduct damaging to business in general, but it is likely to reduce taxpayer co-operation at a time when it is most needed. We are also concerned that some of the proposed reverse charge provisions are disproportionate, for example the £1,000 de minimis on transactions in the affected goods. Since from reported cases the normal size of transactions involved in the fraud is in tens of thousands of pounds, we question whether such a low limit is appropriate, since it will affect (as a purchaser) the vast majority of businesses in the country. As has already been seen, disproportionate measures risk leading to litigation with innocent businesses, when all efforts should be spent in combating the fraudsters themselves and maximising taxpayer cooperation.

Policy recommendations

- i. Government needs to ensure that the proposed reverse charge mechanism to counter MTIC fraud is designed to be both proportionate to the problem and fair to those innocent traders who may suffer damage.
- ii. We believe that tackling MTIC successfully also requires other measures. There are two proposals which we have raised already in discussions with HMRC:
 - a. The input tax 'credit limit' Once a business is VAT registered, it can recover all the VAT it incurs on its costs, with no restriction on the amount (subject to the normal rules and partial exemption etc). One feature we have noted in reported court cases is that relatively small businesses, innocent or otherwise, involved in a fraudulent supply chain have then claimed input VAT on purchases greatly in excess of their historic trading levels.

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A 'credit limit' would impose a monetary restriction on the input tax that each VAT-registered business could reclaim in an accounting period. It would be set at an amount that in the normal course of events the business would not reach, with a genuinely fast-track clearance procedure for businesses to apply for an increase, perhaps for abnormal transactions such as a property purchase. The purpose would be to restrict the willingness of 'middlemen' (innocent or otherwise) to become involved in such transactions and thus reducing the scope of the fraudster to sell the goods and charge VAT. If the middleman knew that he would not be able to recover the VAT automatically through his VAT return, but at best would face a lengthy enquiry from HMRC for exceeding his credit limit, he would be unwilling to enter into the deal. It would, however, require HMRC to be both prompt and efficient in dealing with requests for an increase; otherwise they would be in breach of EC law.

- b. The 'origin system' - This is a much longer term solution, and was favoured by the Commission over the current system introduced in 1993. Whilst from an operational viewpoint, it would stop MTIC fraud, it would require Member States firstly to set up new systems to exchange information and make refunds to businesses promptly, and secondly it would need to be proof against other possibilities of fraud which we have raised with HMRC. An origin system that required businesses to account for output tax on intra-EC supplies, whilst not permitting prompt input tax deduction, would have a negative effect on cross-border trade, and could be seen as discriminatory. Whilst we are aware of the political objections, operationally we see the origin system as the longer-term solution most likely to end the fraud.

CONCLUSION

The measures in this submission represent a comprehensive programme to improve the UK tax system for the benefit of all its stakeholders. Tackling tax complexity, which in turn creates uncertainty, increases administrative costs and undermines trust should, be a key priority. In addition, the 'trust gap' needs to be addressed and further measures to combat criminal fraud of the VAT system. We are keen to work with HM Treasury and HMRC on the areas that we have identified to help improve the tax system.

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FURTHER CONTACT

For any further enquiries please contact:

Frank Haskew
Head of the Institute Tax Faculty
E-mail: frank.haskew@icaew.co.uk
Tel: 020 7920 8618

Luke Herbert
Public Affairs Manager
E-mail: luke.herbert@icaew.co.uk
Tel: 020 7920 8695

THE 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 <http://www.icaew.co.uk/index.cfm?route=128518>.