



The Future of Taxation in the UK

ICAS Tax Board

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Introduction

There has been considerable uncertainty in recent years, for businesses and individuals, following the outcome of the EU referendum and the prolonged Brexit process. The election of a new Government has ended one phase of Brexit, with the UK formally leaving the EU at the end of January 2020 but it has not ended uncertainty as no agreement has yet been reached on the precise nature of UK's future relationship with the EU.

The coronavirus pandemic has added a whole new layer of uncertainty. However, it may also present the Government with an opportunity to generate public support for tax reform to address some of the issues mentioned in this paper. This has previously been difficult to achieve but the aftermath of the pandemic, with strong public support for the NHS, might be the ideal moment for a public debate about who should pay tax and how much they should contribute.

At the same time there have also been significant changes in the business and broader societal environment, most notably linked to increasing digitalisation and developments in AI. Older 'bricks and mortar' businesses have struggled to compete against new global online businesses. The growth of the 'gig' economy has presented opportunities for some but led to exploitation of others.

Taxation sometimes struggles to keep up, both in policy terms and in tax administration. International discussions are in progress to try to resolve how to tax the digital economy; in the meantime some jurisdictions, including the UK, are introducing unilateral interim Digital Services Taxes. Taxing workers in the gig economy also presents challenges. The legislation dealing with tax administration has not kept up with digital developments and is no longer fit for purpose.

The UK also has an overly complex tax system which individuals struggle to understand; adequate support from HMRC can be hard to obtain. The UK government and HMRC have enjoyed considerable success in reducing tax avoidance in recent years. However, there remains a perception that there has been widespread abuse, which contributes to a sense of unfairness.

This paper has been prepared by the ICAS Tax Board to put forward recommendations for addressing key issues affecting the future of taxation in the UK – and the benefits we believe will flow from adopting them. We have considered the following areas:

- Tax and the common good
- Making effective tax policy
- Devolving tax powers across the UK
- Professional relationships – regulation of the tax profession?
- Improving tax administration
- Going digital
- Agents and taxpayers – working together with HMRC
- Corporation tax and multinational enterprises
- Income tax, NICs and workers
- VAT in a post-Brexit environment
- Environmental taxes – adapting to changing conditions.

These recommendations were agreed by the ICAS Tax Board in 2020 and inform the work of ICAS Tax. However, they will be reflected upon and revised to reflect economic, social and political developments.

ICAS members are invited to give us their views on these recommendations by emailing tax@icas.com or login to the CA Connect forum, an area exclusive to members, where thoughts may be shared and discussed with fellow members. There are also opportunities to join ICAS tax committees to discuss these recommendations and many other tax policy and practical matters.

Tax and the common good

Recommendations

- Promote public discussion of tax and its contribution to the common good
- Be transparent about the need to raise revenues and the role of tax in paying for public services
- Avoid introducing more complexity through opaque tax measures
- Shift the focus from tax avoidance to tackling tax evasion
- Make decisions on investment in tax systems which are not solely aimed at reducing HMRC costs but also take account of the impact on the wider economy.

There should be a public discussion exploring the role of tax in supporting public services and contributing to the common good. The government should facilitate this discussion through greater transparency about the link between raising tax revenues and paying for improved public services. Media reporting has concentrated on the need for taxes to be paid by large businesses and wealthy individuals, but the public debate should also cover how, and to what extent, everyone should contribute.

In recent years governments have been unwilling or unable to increase the main revenue-raising taxes but have still needed to raise revenue; the result has been opaque tax changes and a lack of transparency about revenue raising. This has contributed to increasingly complex and lengthy tax legislation, which makes it harder for taxpayers (particularly unrepresented ones) to understand and comply with their tax obligations.

Lack of understanding of an overly complex system, combined with a perception that there has been widespread abuse, has also contributed to a sense of unfairness amongst the public which undermines voluntary compliance. Examples of abuse and problems with the international tax system have been widely publicised but far less publicity has been given to successes in combatting tax avoidance, or to the work of the OECD (supported by the UK government) to reform international tax.

In recent years the government and HMRC have in fact enjoyed considerable success in reducing tax avoidance through a variety of measures. The latest estimates of the tax gap indicate that avoidance only accounts for £1.8 billion whereas far more is accounted for by criminal attacks (£4.9 billion), evasion (£5.3 billion) and the hidden economy (£3.0 billion). There needs to be a shift in focus to address these.

There will always be costs associated with running the tax system. However, a balance needs to be struck between the costs imposed on taxpayers and costs incurred by HMRC. The trend in recent years has been to reduce HMRC costs but at the expense of businesses and taxpayers, with potential adverse consequences for the wider economy and for public support for the tax system. PAYE, VAT and more recently Self Assessment have always involved some cost to taxpayers, but RTI and MTD have shifted the balance further. For MTD, in particular HMRC is no longer providing any free online system for any taxpayers (even the smallest) to use.

The benefits of adopting our recommendations

- Enabling an honest public debate about who should pay tax and how much they should pay
- Improving visibility of spending and tax decisions and the link between them
- Discouraging tax avoidance and encouraging voluntary compliance, leading to further reductions in the tax gap
- Strengthening trust in the tax system
- Reversing the trend of increasing tax compliance costs for taxpayers – and hence improving the broader economy.

Making effective tax policy

Recommendations

- Maintain a single fiscal event
- Ensure that more consultations adopt all stages of the 2011 consultation framework – and act upon the responses
- Issue ‘roadmaps’ to set out a clear strategic path for different areas of taxation
- Avoid piecemeal, reactive policy-making to facilitate tax simplification.

A single fiscal event facilitates good consultation, which in turn assists the development of effective tax policy. The Autumn Budget and associated timetable for consultation, draft legislation and Finance Bill should be retained. ICAS supports the principles set out in the 2017 policy paper ‘The new Budget timetable and the tax policy making process’ which were designed to increase predictability, stability and simplicity in the UK tax system and to address concerns that tax policy making was often piecemeal and reactive. A single autumn fiscal event is also essential to support the devolved nations in making effective tax policy.

The five stage approach to consultation set out in the 2011 ‘Tax Consultation Framework’ is effective when adopted in full. The government, HMT and HMRC should ensure that more consultations include all five stages; omitting Stages 1 and 2, which frequently happens, deprives the government of valuable stakeholder input in clarifying the objectives, identifying the options for implementing them and developing a framework for implementation.

The 2010 ‘Corporate tax roadmap’ should be taken as a model for setting tax policy for the future. It set out the government’s long term approach to the corporate tax regime and for several years there was clarity and consistency around the direction of corporate tax policy.

A new roadmap for corporate tax is long overdue. However, clear tax strategies also need to be developed for other parts of the tax system – and to address long term challenges. These include:

- the growth of the gig economy and the workplace of the future
- removing incentives for tax driven incorporations
- making devolved taxes work effectively, given that they interact with UK taxes
- strategic direction for capital taxes and their interaction with taxes on income
- VAT in a post-Brexit world.

An effective approach to tax policy making could also contribute to the simplification of an excessively complex tax system – or at least to preventing further complexity being added. Piecemeal, reactive policy-making inevitably results in greater complexity, particularly when overall tax revenues need to be maintained.

The benefits of adopting our recommendations

- Facilitating a workable consultation timetable based around one fiscal event
- Supporting the proper use of the devolved tax powers in Scotland and Wales
- Clarifying policy objectives and increasing the likelihood of effective legislation which is less likely to need retrospective correction
- Providing taxpayers with certainty and stability so that they can plan with confidence; for businesses this encourages and maintains investment in the UK and for individuals it facilitates planning for life events, like retirement
- Offering the possibility of meaningful simplification in the longer term.

Devolving tax powers across the UK

Recommendations

- There should be a logical and consistent strategic framework for the devolution of tax powers across the UK
- Closer working between Westminster and devolved governments should be encouraged to ensure that UK tax decisions take account of the consequences for devolved taxes
- A more realistic timeframe for UK and devolved Budgets should be put in place
- A commitment to hold the UK Budget early in the autumn would assist devolved governments.

A number of tax powers have been devolved in recent years to different regional governments; however, this has raised questions about whether the approach to tax devolution should be more consistent across the UK. For example, is it sensible to devolve varying tax powers to different parts of the UK? Corporation tax is being devolved to Northern Ireland but has not been devolved to Scotland or Wales. Income tax rates have been devolved (but not in the same way) to Scotland and Wales - but have not been devolved to Northern Ireland.

There appears to be little central coordination of the powers devolved; nor is there adequate consideration of how devolved rate setting affects the underlying tax base. For instance, the UK basic rate of income tax (20%) is used for giving tax relief at source but in Scotland the relevant rate may be the intermediate rate (21%). There are practical procedures in place to assist with administration but, longer term, proper consideration needs to be given to how devolved tax powers interact with the UK tax framework, and whether the UK framework adequately supports devolution. Ideally, there should be a logical and consistent strategic framework for the devolution of tax powers across the UK.

It is sometimes suggested that NICs are simply another tax and should be merged with income tax, although many members of the public continue to believe that NICs pay for healthcare and pensions. Various government commissioned reviews have illustrated that merging the two would not be straightforward. Devolution adds further complexity because key elements of income tax (the rates and thresholds) are devolved but NICs are

reserved. There has been considerable work by the Office of Tax Simplification (OTS) in recent years to examine how income tax and NIC processes could be aligned to improve administration, but a different approach may be required as the two charges increasingly diverge from one another. Divergence manifests itself in the NIC thresholds and their interaction with the income tax higher rate threshold. It also arises at a policy level: in England, in addition to suggestions for merging NICs and income tax, it has also been proposed to 'hypothecate' NICs and increase them specifically to fund healthcare. This appears odd in Scotland because healthcare is a devolved competence whilst NICs are reserved.

As a result of devolution and the overlap between devolved and reserved matters, the UK should also consider its processes for implementing new tax policy and introducing tax legislation. Something that initially appears to relate to reserved tax may, on closer inspection, affect a devolved policy (whether tax or a related matter, such as the apprenticeship levy). This requires closer working between Westminster and the devolved administrations to ensure that UK tax decisions take account of the consequences for devolved taxes.

A realistic timeframe for UK and devolved Budgets should be put in place; this may require a more formal process, designed to enable maximum collaboration between governments. As a starting point a commitment to hold the UK Budget early in the autumn would assist the devolved administrations in preparing and presenting their own Budgets. It would also allow adequate time for proper scrutiny, which would support accountability in the devolved jurisdictions.

The benefits of adopting our recommendations

- Reducing the risk of unintended consequences arising from a failure to consider the impact of UK changes on devolved matters
- Encouraging better public understanding of tax policy and tax collection across the UK and how these are used to support public spending
- Providing adequate time for devolved Budgets to be presented and properly scrutinised, which would support accountability in the devolved jurisdictions.

Professional relationships – regulation of the tax profession?

Recommendations

- HMRC should recognise that the agent is employed to act on behalf of the taxpayer, whilst also having a relationship with, and responsibilities to, HMRC
- HMRC's work with professional bodies on an Agent Strategy should be reinstated and developed
- In the short term the unregulated sector should be required to operate to regulated sector standards and HMRC should fully utilise its existing powers to exclude agents who behave inappropriately
- In the longer term the aim should be that all tax agents should be qualified and belong to one of the main professional bodies.

HMRC and agents need a good working relationship to facilitate taxpayer compliance. Trust and respect between agents and HMRC staff are vital, as is respect for the different relationships between the three parties: taxpayer, agent and HMRC.

Relationships between the three parties may not always have cut and dried boundaries. Some taxpayers may feel comfortable dealing directly with HMRC and will never use an agent or will only use one occasionally to deal with particular transactions; others will want an agent to handle all their tax affairs and to deal with HMRC on their behalf. Agents who are being paid to act for taxpayers will have contractual terms in place, governing the relationship with their clients.

Tax agents also have a relationship with, and responsibilities to, HMRC. They should conduct themselves in a professional manner, but their duty of care is to their client, the taxpayer. HMRC needs to recognise this and understand that whilst agents support compliance, they do not have a contractual relationship with HMRC. For those agents who are members of professional bodies, certain standards of conduct are required; in relation to tax these standards are set out in Professional Conduct in Relation to Taxation (PCRT). HMRC had been undertaking some work with the professional bodies on an Agent Strategy; this project should be reinstated and developed.

In the UK there is no restriction on the provision of tax services – anyone can offer them. Members of the main professional bodies must meet certain standards (including having adequate professional indemnity insurance and undertaking continuous professional development); if they fall short a client can complain to the relevant body and disciplinary action can be taken where appropriate. HMRC can also report members to their professional body but currently only makes limited use of this power.

Whilst unqualified agents should comply with HMRC's 'standard for agents' this does not fully replicate professional body standards; HMRC should also enforce these more limited standards by imposing sanctions on those who fail to comply. In the worst cases HMRC should fully utilise its existing powers to exclude agents from access to HMRC systems.

It would be helpful to have a clear decision on whether some form of regulation of the tax profession is to be introduced or not; it is very difficult, if not impossible, to enforce standards when anyone is permitted to act as a tax agent. We recommend that the long term aim should be to require that all tax agents should be qualified and should belong to one of the main professional bodies. There should be a transitional period, perhaps involving some form of affiliated status, to allow existing agents to adapt to the change.

The benefits of adopting our recommendations

- Developing better working relationships between HMRC and agents to improve compliance
- Ensuring adherence to professional standards by all agents and reducing the risk of taxpayers appointing a poor agent
- Improving trust in HMRC and in tax agents, which supports voluntary compliance.

Improving tax administration

Recommendations

- Bring together all tax management and administration provisions in a new Taxes Management Act
- Bring the taxes management legislation up to date to take account of increased digitalisation
- Make the legislation more user-friendly by adopting the Tax Law Rewrite approach
- Ensure that HMRC is properly resourced
- Provide adequate HMRC service levels and support for all taxpayers.

We strongly believe that trust in the UK tax system can be developed and maintained only if taxpayers and their advisers can readily understand HMRC powers, deterrents and safeguards. Transparency should be a key feature but the legislation dealing with tax administration is currently scattered across various statutes, making it difficult for taxpayers to access and apply to their own circumstances. It also has not kept up with technological developments, so it is no longer fit for purpose. Piecemeal attempts to patch up the system, such as the recent announcement of legislation on automated processes, do not address the underlying problems.

The time has come for a consolidation of all tax management and administration provisions in a new Taxes Management Act. In producing this the opportunity should be taken to update the legislation to take account of digital developments and to rewrite it in the more user-friendly style which the Tax Law Rewrite project applied to other important tax statutes.

A well-resourced and efficient tax authority is essential for the smooth running of tax administration. Reductions in HMRC headcount and diversion of resources to deal with Brexit have caused problems for agents and taxpayers, particularly businesses and individuals who are not large enough or wealthy enough to have an HMRC Customer Compliance Manager.

Inability to obtain appropriate support from HMRC undermines confidence in HMRC's ability to deliver a fair and effective system. It also increases compliance risks because many taxpayers (not just those dealt with by HMRC's Large Business and Wealthy units) encounter complex tax problems, but those with limited resources

currently find these very difficult to resolve. Named points of contact at HMRC need to be provided for a broader range of agents and taxpayers. For others, HMRC's helplines need to work better and there must be effective escalation of complex queries to the appropriate HMRC specialist.

Digitalisation should not be used to reduce HMRC resources further, without proper consideration of the impact on HMRC service levels: some of any resources freed up, should be redirected to providing adequate service levels and support for all taxpayers.

The benefits of adopting our recommendations

- Improving understanding of HMRC powers deterrents and safeguards will develop trust and support voluntary compliance
- Making it easier for taxpayers and agents to access relevant legislation and to apply it correctly to their own circumstances will reduce non-compliance
- Ensuring that the tax system is perceived to be fair builds confidence in HMRC
- Providing adequate HMRC support and service levels for all taxpayers and agents will reduce compliance risks and improve voluntary compliance.

Going digital

Recommendations

- Provide a digital roadmap to set out how digitalisation of tax will progress for business and personal tax
- Ensure that the timetable for implementation will allow for new systems to be robustly tested with a pilot covering a complete 'cycle', which anyone can join
- Clearly set out the wider benefits taxpayers can expect from digitalisation
- Enable agents to see and do everything their clients can see and do; this must be built into all new systems from the start, so that agents can properly support their clients
- Make digital services so good that everyone who can 'go digital' will want to use them.

Increasing digitalisation is not confined to the UK tax system; tax authorities around the world are adopting a digital approach. However, in contrast to some jurisdictions, the UK starting point is a complex tax regime developed over many years – with legislation which pre-dates the digital era and is often inadequate for dealing with digital developments. This background needs to be taken into account when developing mandatory digital options in the UK.

ICAS supports the Making Tax Digital initiative as something with longer term potential for streamlining the interaction between taxpayers and HMRC. However, it is important to get implementation right and to proceed at the right pace, so that taxpayers see the wider benefits of going digital, rather than simply incurring costs to meet a tax requirement. Mandated digital interaction on a short timescale, as experienced with compulsory MTD for VAT, is not necessarily best for business. One size does not fit all; different businesses need different levels of digitalisation for maximum efficiency.

Lessons need to be learned from the introduction of MTD for VAT before MTD for business income tax is made mandatory. MTD for VAT was only mandatory for businesses with taxable turnover above the VAT threshold, whereas MTD for business income tax will affect much smaller and less sophisticated businesses (subject to any threshold which might be included in the rules).

Income tax returns are also far more complex, and the complexities make quarterly reporting difficult. Ideally, significant simplification would take place before MTD is extended. Work is also needed on the interaction between business income tax and personal income tax (and the Personal Tax Account and Business Tax Account). Whilst work on business income tax and the BTA has progressed, the same is not true of personal income tax (and the PTA), where work has been put on hold, leaving things in limbo and the system frequently not functioning properly.

If MTD is also to be extended to corporation tax this should take place in a reasonable timeframe. Numerous issues which would need to be addressed ahead of implementation were raised in the informal consultation meetings which took place in 2017. It is essential that a proper consultation should take place on the scope and details, followed by legislation and then at least a one year pilot (in which any company which wants to can take part).

We do not support mandatory 'online everything' in the tax system. Digital services should be accessible to everyone and so good that everyone who can 'go digital' will want to use them. There must also be proper alternatives for the digitally excluded and adequate support for the digitally challenged.

The benefits of adopting our recommendations

- Providing a robust and cost-effective tax administration
- Offering digital tax administration that taxpayers will want to use, and which flows from their business systems
- Integrating business and personal income tax digital systems, to facilitate compliance and provide a 'one stop shop' for tax compliance
- Improving public support for tax digitalisation by ensuring it is not viewed as imposing additional costs and burdens solely to meet tax obligations.

Agents and taxpayers - working together with HMRC

Recommendations

- The taxpayer's right to appoint an agent (under the HMRC Charter) should be supported by HMRC in practice
- Agent access needs to be properly designed and built into all new HMRC online forms and systems from the beginning
- The tax system should reflect the diversity of taxpayers and should be accessible to all members of the taxpaying community
- Agents should be able to see and do what their clients can see and do, so they can act effectively on their behalf
- Agents and taxpayers should have timely access to properly resourced helplines for routine issues and to relevant HMRC experts when required.

Tax agents are vital to the effective operation of the UK tax system; this should be properly recognised within HMRC and reflected in HMRC practice. Agents support tax compliance by helping taxpayers to get their tax affairs right; they make complex tax systems workable for businesses and individuals and reduce the risk of unexpected tax costs for all taxpayers. HMRC and agents need a good working relationship to facilitate taxpayer compliance. Trust between agents and HMRC staff needs to be maintained and developed.

The tax system should reflect the diversity of taxpayers and should be accessible to all members of the taxpaying community; in many cases this will mean access through agents, which should be properly supported by HMRC. 'Your Charter' states that taxpayers are entitled to appoint an agent to represent them and that HMRC will deal with an authorised agent. This should mean that agents are able to see and do what their clients can see and do, so that they can act effectively on their behalf. Agent access needs to be properly designed and built into all new online forms and systems from the beginning, not added as an afterthought.

The process for obtaining the taxpayer's authorisation of an agent should not be too onerous and there should be alternatives to 'digital handshakes' for those who cannot (or do not wish to) engage digitally with HMRC. In general, a taxpayer who appoints an agent will wish to delegate

the handling of their statutory obligation to report income and self-assess their tax liabilities to the agent. Many taxpayers who appoint agents do not want to interact with HMRC. Security is important but making it unduly difficult to authorise an agent prevents taxpayers exercising their rights under the Charter or may lead to the adoption of insecure 'workarounds'.

Agents and taxpayers need access to HMRC support and (where appropriate) to relevant experts within HMRC. Helplines and online forums need to be properly resourced and able to deal quickly and efficiently with routine questions and issues. Escalation routes for more complex matters need to work effectively.

HMRC should introduce a designated HMRC contact for all larger agent firms – whose clients account for substantial amounts of tax and whose affairs are often complex. This contact would have a similar role to a Customer Compliance Manager working with large companies in ensuring that access to relevant HMRC expertise is available on a timely basis. We appreciate that it is not feasible to give everyone a designated contact but if there is to be trust in the tax system, and a perception of fairness, all taxpayers and their agents should have adequate access to HMRC, when they need it. Escalation routes from agent and customer helplines therefore need to be considerably improved. For smaller agents an enhanced and improved Agent Account Manager service could be a useful starting point.

The benefits of adopting our recommendations

- Providing full support for the taxpayer's right to appoint an agent should help to promote trust in the tax system and improve voluntary compliance
- HMRC and agents interacting efficiently, making a complex tax system workable for businesses and individuals
- Reducing the risk of unexpected tax costs for taxpayers and appropriate utilisation of tax reliefs
- Giving all agents and taxpayers adequate access to HMRC and reducing complaints against HMRC.

Corporate taxation and multinational enterprises

Recommendations

- Provide a roadmap setting out the government's long term policy intentions for the taxation of multinationals
- Support the work of the OECD on proposals for the reform of the international tax system
- Avoid introducing further unilateral tax measures, wherever possible
- Where unilateral measures are deemed to be essential to protect the UK tax base, these should be introduced on a temporary basis and replaced once international agreement has been reached
- Carry out proper consultation on proposals for Making Tax Digital for corporation tax – and bear in mind the interaction with digital tax systems in other jurisdictions.

Large businesses and multinational enterprises play a vital role as major contributors to the UK economy, job creators and collectors of tax revenues (VAT, income tax and NICs). Whatever the final outcome of Brexit, it is important that UK tax policy supports the government's aim of ensuring that the UK remains an attractive place for multinationals to do business.

The tax system needs to be flexible to deal with change, but companies also need to be able to plan for the future with confidence. The Brexit referendum in 2016 has resulted in a long period of uncertainty for business; it is important that this uncertainty is not intensified by constant, unpredictable changes to the tax system. Large businesses would welcome a roadmap setting out the government's long term policy intentions for the taxation of multinationals.

The introduction of unilateral measures such as the Diverted Profits Tax, or the Digital Services Tax, imposes additional compliance burdens and is likely to give rise to double taxation. An international approach to tackling the taxation challenges arising from multinational companies is preferable, where this can be achieved. The government should continue to support the work of the OECD on proposals to reform the international taxation system. Where unilateral tax measures are deemed to be essential to protect the UK tax base, these should

be introduced on a temporary basis and replaced once international agreement has been reached.

It should be noted that much tax administration is 'outsourced' to MNEs, with new measures adding to this – for example, the proposed extension of IR35. The Corporate Criminal Offence and the Directive on Administrative Cooperation (DAC 6) are also very widely drawn: risk assessing and putting in place extensive procedures to comply is a considerable burden and has a significant impact on the cost of doing business.

In implementing Making Tax Digital (MTD) for corporation tax, the UK should learn from other countries, which are increasingly adopting a digital approach to tax administration. The UK needs to bear in mind the interaction with digital tax systems in other jurisdictions because multinationals operate in many countries. If interaction is not considered the cost of compliance is increased. There should be a full consultation on the UK MTD proposals followed by a pilot which all companies can join from the beginning, and which covers an entire tax cycle.

Extensive digital reporting requirements are being imposed – with increasing amounts of data being made available to tax authorities internationally. It is not currently clear how MTD for CT might work in the UK but if it means that HMRC receives far more data some of the current reporting requirements should be removed.

The benefits of adopting our recommendations

- Providing clarity on the government's future taxation plans allows businesses to plan for the future with confidence which should help to maintain and attract investment in the UK
- Developing and implementing an agreed approach to international taxation minimises administrative compliance burdens and helps to avoid double taxation
- Aligning MTD for multinationals with digital systems in other jurisdictions will reduce compliance burdens and improve reporting
- Implementing MTD for CT after proper consultation and with a full pilot will minimise disruption and improve efficiency.

Income tax, NICs and workers

Recommendations

- Better alignment of taxation and employment law
- The government should continue to implement commitments made in the 2018 Good Work Plan
- The treatment of employed and self-employed workers should be more closely aligned by introducing changes to self-employed NIC rates and to expenses rules
- Additional resources should be made available for tackling modern slavery and the exploitation of gig economy workers.

This area of the tax system is riddled with distortions, which have also been highlighted by the provision of the coronavirus schemes. An individual worker may prefer to be self-employed rather than employed because NICs will be lower and the expenses rules are more generous. Lower corporate tax rates and lower taxation of dividends incentivise many businesses to incorporate. Sometimes, however, workers are forced into false self-employment (or into setting up their own personal service companies) because the users of their services want to avoid employers' NICs and employment rights. The growth of the 'gig' economy has also seen increasing numbers of individuals whose tax status can be hard to determine, due to the number of roles in each individual's 'portfolio' and the lack of alignment between tax and employment law.

Attempts to tackle problems in this area – recent examples include changes to the taxation of dividends, some restriction of reliefs on incorporation, IR 35 and the off-payroll working rules – have increased complexity and produced some unintended consequences. The proposed extension of the off-payroll working rules to the private sector has been delayed due to coronavirus and its damage to the economy; we note too, the recent report from the House of Lords Finance Bill Sub Committee on this topic. We believe that the fundamental issues of taxpayer behaviour, employment ethics and falling NIC revenues urgently need to be addressed.

As a starting point employment law and taxation need to be more closely aligned – allowing for greater certainty around the boundaries between self employment and

employment. The government's 2018 Good Work Plan stated that it would bring forward detailed proposals on how employment status frameworks for employment rights and tax could be aligned. The plan also committed the government to legislating to improve the clarity of the employment status tests. Proposals and draft legislation should be published as soon as possible – and should recognise the distinction between those who are genuinely self employed entrepreneurs and those who are really acting as employees.

Increased clarity around employment status needs to be accompanied by measures to improve the alignment between the taxation of employed and self-employed workers. Retaining Class 2 NICs avoided increasing the gap between employees and the self-employed but self-employed workers still continue to pay significantly lower rates of NICs than employees. The self-employed also enjoy more generous relief for expenses. Due to changes to state benefit entitlements it is difficult to continue to justify these differences. Addressing both these distortions should be a short term ambition and could be achieved without significantly increasing complexity.

In the longer term, the cost of employer NICs needs to be addressed, preferably alongside consideration of the likely consequences of increased use of AI and robotics. Currently, the cost of employer NICs is key to exploitative practices in the gig economy and to illegal modern slavery; additional resources should be made available for tackling these. In future AI could reduce the number of workers required, with serious consequences both for tax revenues and wider society. We recommend that full and proper consideration is given to how to address these issues.

The benefits of adopting our recommendations

- Providing greater clarity on employment status for employers and workers
- Reducing the role of tax in pushing individuals towards self-employment for the wrong reasons
- Improving alignment of the taxation of the self-employed and employees, making clear the link between paying tax and NICs into the system and receiving state support
- Reducing exploitation of vulnerable workers.

VAT in a post-Brexit environment

Recommendations

- Allow time for ongoing VAT administrative changes to be fully embedded
- Convert all existing VAT measures into UK law at the time of leaving the EU
- VAT simplification measures should be the priority after Brexit
- If devolution of VAT is a potential future option, there should be a careful assessment of the potential consequences.

Post-Brexit (after the implementation period), when the UK is no longer subject to EU VAT law, there is the potential for major changes to VAT. Whilst existing VAT law will be mirrored on Day 1 of Brexit, over time there will be no barrier to VAT being changed or even swept away. Changes could apply across the UK or could potentially involve some devolution of VAT powers. We are not referring to Northern Ireland in this section, as full details of the arrangements with the EU are still to be finalised.

VAT is an efficient tax that raises a significant amount of revenue. However, the legislation is complex, it is a much litigated tax, and we caution against any early significant changes in VAT after Brexit. There are ongoing administrative changes that need to be fully implemented, including Making Tax Digital for VAT, the forthcoming VAT construction industry domestic reverse charge, and there will also be essential post-Brexit changes such as postponed accounting.

Simplification of VAT is possible, as set out by the Office of Tax Simplification. ICAS believes that the OTS report identifies numerous aspects of the VAT regime which could usefully be simplified. As its report notes, whilst the UK remains within the EU there are constraints on what it can do. After Brexit, it should be easier to undertake radical reform; there may be a case for considering reform in stages, but ICAS believes that the priority should be simplification measures.

In a post-Brexit world, there is also scope to consider devolution of VAT powers within the UK. However, before adopting this approach, further work should be undertaken to inform decision making in three areas:

- First, VAT has various functions, including generating government revenues, encouraging or discouraging certain behaviours, and/or supporting the economy and its growth. There should be an examination of how devolution of VAT could affect these. For example, if VAT rates were to be cut by one administration, would this trigger cuts across the UK, which would nullify the competitive advantage and erode revenue? Or, would rate cuts instead boost economic activity for everyone?
- Secondly, an analysis of the burdens that could be imposed on businesses is essential. VAT is designed to collect revenue on the 'value added' at all stages in a production chain and is most effective across an integrated market. Devolution could lead to different VAT regimes, and hence to increased complexity and increased burdens on business. From the business perspective, it is therefore important to consider how the devolution of VAT powers could affect the efficiency of the UK single market and how any business burdens could be minimised.
- Thirdly, if devolution leads to different VAT regimes, it will also lead to tax planning. A competitive environment, from a tax perspective, encourages taxpayers to use the regime that will minimise costs. This may appear helpful initially but if all jurisdictions aim to be competitive it may lead to all their tax revenues being reduced. It also sends an ambiguous message in relation to tax avoidance.

A full analysis of the potential consequences of VAT devolution is needed to inform decision making.

The benefits of adopting our recommendations

- Allowing businesses to fund and resource the implementation of ongoing administrative changes before imposing additional costs by embarking on radical change
- Reducing ongoing compliance costs and decreasing the risk of incurring penalties by simplifying some of the most complex areas of VAT
- Enabling an understanding of the potential consequences of VAT devolution.

Environmental taxes – adapting to changing conditions

Recommendations

- The aim of any environmental tax should be to drive behavioural change and deliver benefits for the environment
- Environmental taxes should not be designed primarily to raise revenues
- Develop a framework for assessing the case for new environmental taxes
- Engage with the public about proposed new environmental taxes and the rationale behind them.

Due to societal changes, technological developments and environmental issues there may be strong arguments for introducing new environmental taxes. These should not be primarily intended to raise revenues; the intention should be to change behaviour and deliver benefits for the environment.

The ICAS definition of 'environmental taxes' is:

- taxes with the primary objective of encouraging environmentally positive behaviour change, and
- structured in relation to environmental objectives, for example: the more polluting the behaviour, the greater the tax levied.

The government should develop a framework for assessing the case for new taxes to ensure that they are well-designed and achieve the desired objectives. Questions to be addressed should include:

- Why is a new tax needed?
- What is its primary objective?
- Is there a better way of achieving the objective?
- What are the key features of an effective tax?
- Can the tax be collected without imposing disproportionate administrative burdens?
- Could there be unintended adverse consequences? If so, how could these be mitigated?

The primary objective of an environmental tax should be to encourage positive behaviour change. Therefore, it would be counterproductive for government to hope to raise significant revenues from environmental taxes. The key measure of success for an environmental tax

should be the reduction or elimination of environmentally damaging behaviour. A tax which continued to raise significant amounts of revenue over a long period of time would therefore have failed. Initially there could be high yields as those affected adapt to the new regime but if the environmental tax is well-designed receipts should subsequently decline, along with the targeted environmentally damaging behaviour. If everyone is willing to continue to pay high levels of tax, ie the tax does not effectively change behaviour, there will be little benefit to the environment.

If the environmental taxes achieve their aim of changing behaviour and do not produce significant revenues in the long term, this could present problems. For example, fuel duty currently produces revenues – but these will reduce as people switch to electric cars (which currently benefit from some incentives).

It will be important to maintain public engagement with environmental issues and to generate public support for new environmental taxes. The rationale behind environmental tax decisions therefore needs to be explained clearly and there should be meaningful public consultation on the rates and design of any proposed new environmental taxes.

The benefits of adopting our recommendations

- Designing new environmental taxes effectively and reducing environmentally damaging behaviour
- Avoiding undue complexity and disproportionate administrative burdens
- Encouraging public support for new environmental taxes.

The ICAS role

ICAS (The Institute of Chartered Accountants of Scotland) is the oldest professional body of accountants. We represent over 22,000 members who advise and lead businesses. Around half our members are based in Scotland, the other half work in the rest of the UK or in almost 100 countries around the world.

ICAS has a public interest remit – a duty to act not only for its members but for the wider public good. Our technical experts work in a positive and constructive manner to advise policy makers on legislation and to raise issues of importance to our members, individual taxpayers and business.

Taxation is one such area of importance and ICAS has contributed, and will continue to contribute, to tax policy in Scotland, the UK and beyond.

The Tax Board's objectives in discussing the Future of Taxation in the UK are to:

- act in the public interest
- provide constructive input to the authorities, and
- represent ICAS members and students' interests.

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