



Office for Tax Simplification
Comments on the *Review of tax reliefs, interim report*

1. Executive summary

- 1.1. We welcome the Office for Tax Simplification's Review of tax reliefs interim report.
- 1.2. We feel that the methodology adopted is generally correct, except that we do not think taxpayer take-up is necessarily a proxy for the perceived value of a relief.
- 1.3. Progressivity of the tax system as a whole is a key part of reform and we would prefer there to be no losers from simplification at the lower end of the income distribution, or that any who lose out as a result of tax relief changes may be compensated by other means – for example through earmarking funds saved to provide more targeted relief through the welfare system.
- 1.4. It is important to acknowledge that tax law and therefore its simplification cannot be separated from other areas of law, for example National Minimum Wage regulations and welfare benefits. Proposals must therefore be considered in the round, particularly with an eye on future policy developments such as welfare reform.
- 1.5. We have commented on the initial application of the OTS's methodology to a sample of reliefs, to the extent that they may be relevant to people on low incomes.
- 1.6. We have then looked at those reliefs listed in each Annex, commenting on where we

consider we have further contributions to make.

- 1.7. In summary, this paper is a collection of our initial thoughts relating to the current review of tax reliefs, which we conclude by offering further input in those areas within our expertise – particularly those we have highlighted. We look forward to working closely with the OTS as its work develops towards recommendations for simplification.

2. Introduction

2.1. *About us*

- 2.1.1. The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes.
- 2.1.2. The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

2.2. *General comments*

- 2.2.1. LITRG has welcomed¹ the formation of the Office for Tax Simplification (OTS) as part of the Government's overall strategy to change the process of making tax policy.
- 2.2.2. For the unrepresented taxpayer, simplification of the tax system and its interactions with other arms of government would go a long way towards improving their chances of compliance. It should also have cost saving benefits for the administering departments.
- 2.2.3. The challenge of achieving simplification is, however, not to be underestimated and whilst the OTS has clearly made a good start in its initial Review of reliefs, Rome was not built in a day. It may therefore be necessary to break down any proposed changes into short term 'wins' (that is, obvious simplifications which will have little or no impact) and longer term aspirations (which will require more serious thought as to potential impacts on taxpayers and interactions across government).
- 2.2.4. Our comments first focus on the questions about the methodology used in the Review of tax reliefs, then turn to the specific sample of reliefs chosen for the interim report and finally comment on those other reliefs where we think there could be impacts on low-income, unrepresented taxpayers.

¹ See <http://www.litrg.org.uk/News/2010/tax-policy-making>

3. Methodology questions

3.1. **Question 1: Do the criteria set out in Chapter 2 achieve the objective of determining whether a relief is fit for purpose, and whether it can be simplified or abolished?**

3.1.1. In general, yes. But we disagree with para 2.16, second bullet which says:

“Evidence of taxpayer take up, which is a proxy for the perceived value of the relief. This is a function of understanding, complexity and whether the legislation is too tightly focused.”

3.1.2. Take-up is not necessarily a proxy for the perceived value of the relief. A relief that is little known, perhaps because it is highly complex or badly publicised, might be very valuable to those who do find out about it and make use of it. Its value might be greatly enhanced by simplifying it, or publicising it better.

3.1.3. The blind person’s allowance (BPA) is one such example. Its low rate of take-up is probably due to the lack of awareness, perhaps less of the allowance itself than of the ability to transfer it to a spouse or civil partner who may deduct it from his or her income if the claimant’s own income is insufficient to use some or all of it.

3.1.4. TaxHelp for Older People have been campaigning to increase take-up and are continuing to do so. This is a case where awareness of a relief could be increased amongst its likely claimants through co-operative work across government (and indeed working with the voluntary sector), for instance HMRC ensuring that in England and Wales, when local authorities register someone as blind, they are helped to understand the allowance and how it could be claimed by them or their spouse/civil partner.

3.1.5. As BPA has been identified in Annex A of the interim report, we comment further on it below (section 5).

3.2. **Question 2: Are there other criteria that we have not given sufficient weight to in relation to determining simplification?**

Winners and losers, and progressivity

3.2.1. We appreciate that simplification is difficult to achieve without there being some winners and some losers as a result. But in assessing the impact of changes to tax reliefs, it must be acknowledged that a relief worth little or nothing to higher net worth taxpayers may be worth a lot more to those on lower incomes.

3.2.2. We think that the tax system should be progressive across the board.

Simplification of reliefs rather than abolition

3.2.3. Complex reliefs, which for that reason are inaccessible and poorly taken up, could be preserved in a simplified form rather than abolished.

3.2.4. But if a relief is earmarked for abolition and, following on from our progressivity comments,

is found to result in losers in lower income and vulnerable groups, mitigation should be considered by means of compensating them elsewhere. This might not be through the tax system, but by means of a more targeted benefit or credit given elsewhere.

The impact of a change in tax legislation on other areas of law

- 3.2.5. We believe that tax legislation changes should not be considered without looking at the wider impacts on other areas of law. For example, interactions with welfare benefits, and tax credits.
- 3.2.6. In this context, it is necessary not only to consider the current impacts – for example how a change to an income tax relief impacts on tax credits claimants, the regulations for which cross-refer to many areas of the income tax legislation – but also future policy developments. An apparently simple change now in tax law could, for instance, create future complexity if the possible interactions with the new Universal Credit and other welfare reforms are not thought through.
- 3.2.7. The OTS review should therefore consider whether changing tax law to simplify a relief for tax purposes creates more complexity by introducing differences with other areas of law. For example, the National Minimum Wage regulations have been changed with effect from January 2011 to import the income tax definition for qualifying home to work travel. Where there are such interactions, changing the tax law might simplify the tax issue but introduce differences with (or unforeseen impacts on) other law.

4. Chapter 4, applying review methodology to a sample of reliefs

- 4.1. We have considered the 13 specific reliefs sampled in the interim report and comment below to the extent they may be relevant to people on low incomes.
- 4.2. ***CGT private residence relief (potentially retain)***
- 4.2.1. We agree that this valuable relief should be retained.
- 4.3. ***Income tax relief for repair and maintenance of work equipment (potentially retain)***
- 4.3.1. We agree with the interim report's conclusions on this relief, particularly that there might be scope for extension to other industries.
- 4.3.2. We would also suggest considering the following questions:
- Do the figures reflect up-to-date costs of repair and maintenance of tools etc?
 - Should there be a flat rate across all trades?
- 4.3.3. In terms of the second bullet, a flat rate would certainly simplify the relief, but the figure chosen should be such as would ensure there were no losers.

4.4. ***VAT zero-rating etc on certain supplies by and to charities (potentially simplify)***

4.4.1. This is analogous in some ways to zero-rated supplies to disabled people as considered in our 2007 report, '*VAT and disabled people – the case for removing the barriers*'¹. We would suggest the Government investigate the scope to extend support to charities and disabled people, if not through further zero-rating at least by use of reduced rates.

4.5. ***Gift aid (potentially simplify)***

4.5.1. For many years, LITRG has highlighted the complexity of gift aid, in terms of it being available only to taxpayers. We have previously recommended² that the scheme be extended to non-taxpayers, with the possible consequence of splitting the accounting between tax relief and public expenditure.

4.5.2. Furthermore, our 2009 report '*Bureaucracy, expenses and the low-income volunteer*'³ suggested simplification by reforming the gift aid process for expenses which volunteers wish to donate back to the charity (or Community Amateur Sports Club). Currently, the expenses have to be paid then donated back in order to qualify as a gift aid donation, causing unnecessary administration for volunteers and the organisations alike.

4.6. ***Late night taxis home from work (potentially abolish)***

4.6.1. Abolition of this relief would affect employees on low incomes more than those on higher incomes if the tax payable on the taxi ride exceeded the cost of their usual journey home by bus or train, or if abolition caused employers to withdraw the benefit altogether.

4.6.2. The policy objective would seem to be to ensure the safety of employees (particularly female employees) when travelling to or from work at unsocial hours, and the need for that remains. Withdrawal would place low-income employees at greater risk compared with those who could afford their own taxi. This is particularly the case if the employer is also a small business which does not arrange PAYE Settlement Agreements (PSAs), or if use of the taxi is infrequent and unpredictable therefore difficult to estimate for the purposes of a PSA.

4.7. ***NS&I ordinary account (potentially abolish tax-free status for first £70 of interest in any year)***

4.7.1. It is unclear whether the relief still applies to deposits sitting in the residual account mentioned in para 4.146, or if all interest on such deposits (if any) is taxable. If this is to go ahead, it will be important to contact everyone who still has a deposit and explain the

¹ See

<http://www.litrg.org.uk/reports/2007/vat-and-disabled-people-the-case-for-removing-the-barriers>

² See our response to HM Treasury's 2007 consultation

http://www.litrg.org.uk/Resources/LITRG/1_464_Giftaidresponse260907.pdf

³ See <http://www.litrg.org.uk/reports/2009/bureaucracy-expenses-and-the-low-income-volunteer>

situation carefully to them, offering alternatives and making it easy for them to select one.

4.8. ***Luncheon vouchers (potentially abolish)***

4.8.1. We agree with the conclusion of the interim report.

5. **Annex A: Reliefs the OTS plans to include in the next stage of their review**

5.1. Although we have not considered them in full at this stage, we list below those reliefs identified in Annex A where we believe there might be issues for low-income taxpayers and on which we would therefore be pleased to comment further in due course. Our initial thoughts, where relevant, have been noted.

5.2. ***Blind person's allowance, other 'dwindling' tax allowances and complexity of tax rates***

5.2.1. Our 2003 report, *'Disability in tax and related benefits: the case for a modern and coherent approach'*¹ highlighted the problems with blind person's allowance and its failure to reach many of those who would benefit from the support it is intended to offer. We have noted above where much can be done to improve its take up, but if the OTS does come down in favour of its abolition, we believe the Government should set aside equivalent funds to be redistributed in the form of benefits targeted at all sight-impaired disabled people.

Married couple's allowance

5.2.2. It makes a degree of sense if reviewing the blind person's allowance to consider also the married couple's allowance (MCA). The beneficiaries of this relief are dwindling as the years pass, it now being restricted to claimants where one of the couple was born before 6 April 1935.

5.2.3. Whilst we would not want to see the remaining claimants of MCA lose the value of their tax relief, we think the rules could be simplified for those that remain. For example, how many people born before 6 April 1935 either marry or register a civil partnership (few, we suspect)? So there would seem little cost to the Exchequer in abolishing the rule to pro-rate the relief in the year of so doing.

Tax rates

5.2.4. Connected to allowances are tax rates. For many of those on low incomes, a straightforward tax rate structure would go a long way towards simplification. One example of complexity is the tortuous 10% starting rate on savings (effectively a 'relief' and therefore we assume potentially within scope of the current OTS review) which is probably claimed by few who

¹ See <http://www.litrg.org.uk/reports/2004/disability-in-tax-and-related-benefits-the-case-for-a-modern-and-coherent-approach>

are entitled because of its complexity. This is therefore worthy of additional thought, and if not part of the current review, to be flagged for the OTS's future work.

5.3. ***Life insurance policy relief (including top-slicing)***

- 5.3.1. As we understand it, a good number of non-qualifying life policies have been sold (possibly mis-sold) over the years as a form of saving for retirement. They have little value for basic rate or non-taxpayers and the unwitting pensioner encashing a bond triggering a chargeable event gain can find their age allowance restricted even when they would otherwise be on a low income. In that situation, it is an unfortunate feature of the current system that top slicing relief does not come into play.
- 5.3.2. Worse off still are those who have been advised to invest in offshore policies, which have no associated notional tax on encashment. And, particularly in recent years, it seems unfortunate for many that there is no loss relief available (apart from the limited 'corresponding deficiency relief' where a loss is incurred on the same policy which previously triggered a chargeable event gain).
- 5.3.3. A review would therefore be welcome, particularly in the context of the low-income pensioner population.

5.4. ***Payroll giving***

- 5.4.1. Our initial thought is that payroll giving is probably under-utilised and therefore a scheme worthy of promotion rather than abolition. This is particularly in the context of considering ways to boost charitable giving following the reduction in Gift Aid tax relief to charities on imminent expiration of the three-year transitional relief (due to the reduction in the basic rate of tax from 6 April 2008).

5.5. ***Repair and maintenance of work equipment***

- 5.5.1. See comments above.

5.6. ***Seafarers' earnings deduction***

- 5.6.1. Low-income issues could arise and we would be pleased to contribute to the OTS's thinking in due course.

5.7. ***Trade union membership subscriptions***

- 5.7.1. Low-income issues could arise and we would be pleased to contribute to the OTS's thinking in due course.

5.8. ***Employee travel, and treatment of employee expenses generally***

- 5.8.1. The following reliefs flagged in Annex A fall seem to within the general category of 'employee travel': meal provision on cycle to work days; cycles and cyclists' safety equipment; and late night taxis.

- 5.8.2. Rather than consider these in isolation, we think it would be preferable to review employee travel as a whole. Our recent work on National Minimum Wage and travel expenses refers¹, as well as our submissions on welfare reform and Universal Credit².
- 5.8.3. At the same time, it is worth considering the wider issue of employee expenses and claims and their different treatments for income tax and National Insurance. Recently, increased attention has been focused on possible alignment, or even merger, of income tax and National Insurance. We think that there is merit in reviewing the two systems to see where consistency can be achieved.
- 5.8.4. For example, where an employee is not reimbursed employment-related expenses by their employer, such as for business mileage, they can make a claim against their income tax liability for tax relief on the value (although many may not do so because they are not aware they can). However, a similar claim is not available for National Insurance.
- 5.8.5. Allowing such claims would be a simplification and remove an element of unfairness for employees of less generous employers.

5.9. ***Miners' coal***

- 5.9.1. Low-income issues could arise and we would be pleased to contribute to the OTS's thinking in due course.

6. Annex B: Further reliefs the OTS will include in the next stage of their review if time permits

- 6.1. As for those reliefs picked out of the Annex A listing above, although we have not considered them in full at this stage, we list below those reliefs identified in Annex B where we believe there might be issues for low-income taxpayers and on which we would therefore be pleased to comment further in due course. Again, our initial thoughts, where relevant, have been noted.

6.2. ***Welfare counselling***

- 6.2.1. As far as we are aware, a good number of employers provide access to a counselling scheme. Our initial reaction is that the exemption from benefit in kind for employees should be preserved.

¹ See <http://www.litrg.org.uk/submissions/2010/travel-expenses-nmw>

² See (in particular paragraph 3.6ff) http://www.litrg.org.uk/Resources/LITRG/Documents/2010/11/LITRG_response_to_21st_Century_Welfare.pdf

6.3. ***Compensation for mis-sold pensions***

6.3.1. If the OTS has time to consider this relief, we would be pleased to assist with looking at the issues for low-income taxpayers.

6.4. ***Employer-supported childcare***

6.4.1. This is an area in which LITRG maintains significant interest, not just in pure tax terms, but in the linkages with tax credits and welfare benefits. Simplification of childcare support is of key importance in welfare reform. Furthermore, since their introduction, we have been highlighting the pitfalls of childcare voucher schemes for tax credits claimants.

6.4.2. If the OTS does have time to include this area in its review of reliefs, we would therefore have a significant contribution to make.

6.5. ***Inheritance tax, disabled trusts relief***

6.5.1. Although the capital gains tax and income tax reliefs for trusts for the vulnerable are included in Annex C of the interim report (reliefs not to be considered for the time being), we would strongly advise that the inheritance tax relief is not considered in isolation from them.

6.5.2. Indeed, we have been recommending for some time that the reliefs be harmonised across the taxes as it seems illogical for different rules to apply to trusts for disabled beneficiaries for inheritance tax, capital gains tax and income tax.

6.5.3. Again, we would be pleased to submit a separate paper on this subject to the OTS for consideration if they reach the stage of reviewing of the inheritance tax relief listed in Annex B.

7. **Annex C: Reliefs the OTS is not examining further at this stage**

7.1. A number of the other reliefs within Annex C are relevant for low-income taxpayers. If at any stage the OTS review therefore extends to them, we would be pleased to contribute.

7.2. ***Pensions, trivial commutations and other lump sums***

7.2.1. In particular, one area we have been researching and reviewing is trivial commutation of small pensions.

7.2.2. This seems to us an area ripe for simplification. For example, the need to commute a number of small pensions within 12 months of the first creates problems. We have been unable to determine clearly the policy rationale for such a restriction, which seems an unnecessary complication where there is already a monetary limit on the overall amount which can be encashed.

7.2.3. This policy can lead to distortions by, for example:

- forcing the encashment of all policies within a short space of time which might not make financial sense for the taxpayer; or
- forcing the purchase of an annuity in the (not uncommon) situation of a forgotten small pension pot coming to light after the 12 month window has expired.

7.2.4. We would be pleased to submit a more detailed paper on the issues, if it would be helpful to the OTS's work.

LITRG
2 February 2011