

## Improving tax policy making

### Emerging findings—an invitation to comment

#### Background

The Institute for Government, the Chartered Institute of Taxation and the Institute for Fiscal Studies launched our joint tax policy project in April 2016. Our aim is to work together to produce a clear set of recommendations to the Government, Opposition and other stakeholders on how to improve the UK tax policy making process and the process around Budgets. We are looking to launch proposals for reform later in the year.

#### Purpose of this paper

This paper builds on an earlier version which was discussed at a roundtable in late June 2016. That paper drew on our initial desk research and discussions with tax professionals, economists, and representative groups. It also draws on some submissions sent to us as part of the call for evidence we issued [when the project was launched](#). It now incorporates many of the points made at the roundtable.

We welcome further comments on:

- Which of the “areas for future focus” we set out under each theme here are the most important and /or have the most potential to improve the system
- Thoughts on how best to address the issues in those suggested areas

We would welcome any comments by 2 September 2016, if possible, though earlier reactions would be very welcome. Please comment to [tax@instituteforgovernment.org.uk](mailto:tax@instituteforgovernment.org.uk)

#### Emerging findings

In the rest of this paper we set out the emerging findings from our work, and the main questions that they pose. Many people noted that the system for tax policy making has changed considerably since 2010 – and that there have been significant, if patchy, improvements. This is a clear indication that when political incentives change, processes can change, despite their roots in history and tradition. The creation of the Office for Budget Responsibility (OBR) in 2010 is a much more radical step than would be

needed to address many of the concerns raised in this paper, and shows the scope for changing conventional practice when the political incentives are right.

We have grouped the challenges under the following themes:

- **Strategy:** providing a long-term plan for tax policy
- **External engagement:** consultation with practitioners and other external bodies
- **Internal Budget process:** how Budget proposals are developed and tested
- **Legislation and legislative scrutiny:** the role of Parliament in scrutinising tax measures
- **Post-legislative review:** ex post review of tax measures
- **Capability:** the skills and capacity of the HMT and HMRC workforce
- **Public debate:** how public understanding informs or limits tax policy making

It is clear from what follows that these do not stand as discrete issues – so, for example, a clearer overall strategy for the tax system, or for parts of the tax system, would improve both the quality of public debate and external engagement around policy options. Changes to the internal Budget process within government could improve scrutiny and make post-legislative review easier. Reducing turnover and building expertise in Treasury and HMRC staff could improve the quality of consultation.

It is also clear that many improvements require an approach that appreciates that individual elements of tax policy are part of a wider system beyond even tax, and that problems arise when those potential interactions are not understood or identified when tax policy is being made.

## Emerging findings and areas for future focus

### 1. Strategy

No government has yet set out a formal tax strategy for a Parliament. Many of our respondents thought the lack of such a framework encouraged ad hocery.

- The absence of a clear strategy for tax policy makes it hard for outsiders to discern a clear overall direction for a Parliament or an administration; or to understand the government's view of how it wants to use the tax system and when tax is the most appropriate instrument. That creates a tendency to meddle, with changes that make the tax system more complex and less coherent.
- The experience of the 2010 Business Tax Roadmap, setting out the course of tax over a Parliament, has been positive. But in other areas government intentions are unclear, or not pulled together into a coherent narrative – on pensions and on savings, for example. This extends to individual measures where objectives are often unclear.
- There are consequences for consultation and public engagement. There is little public discussion of the options government faces, or understanding of trade-offs; expert response tends to be

siloed and focuses on individual measures, not the bigger picture. The absence of a strategy makes it hard for outsiders to feed in options for meeting government objectives.

- Earlier, more strategic engagement with providers could help improve the impact of Budget measures, for example on measures to promote savings or home buying.
- However, to be useful, an overarching tax strategy for a Parliament would have to constrain a Chancellor's options, reducing their flexibility to respond to events. There would have to be clear political benefits from tying their hands in this way.
- Extending the roadmap approach to other areas might be a more realistic way forward than having a comprehensive tax strategy.

#### *Areas for future focus:*

- How can the government give a better overall sense of direction? Is it realistic to produce an overarching tax strategy for a Parliament?
- If it is not, would it make sense to try to produce more thematic roadmaps to give a clearer sense of direction, building on the experience of the corporation tax/business road maps?
- How may Brexit impact on the perceived need for a clearer sense of direction on tax—and the feasibility of taking a more strategic approach?

## 2. External engagement

There was a general feeling from interviewees, and especially amongst practitioners, that where the principles set out in the 2010 *New Approach to Tax Policy Making* are followed, both informal and formal consultation on tax policy proposals has improved – but could benefit from further improvement.

- There is a widespread feeling that consultations are rarely “open”, in the sense that decisions have been made, justified on the basis of market sensitivity. Consultation is therefore primarily about technical design issues. Lateness has often been justified on the basis that proposals were market sensitive, but there is a feeling this risk is exaggerated. It can be hard for consultees to understand the purpose of measures, and greater transparency on this would improve the quality of consultation.
- It is important to learn from examples of good consultations where views were invited at an early stage of policy development. The consultation around [the statutory residence test](#) was cited as an example where the consultation process had resulted in legislation which, although long, catered for people with complex circumstances (an alternative view was this was now too complex); or the way in which the Treasury had consulted on options for [the tax treatment of pensions contributions](#), even though the more general approach to tax policy on pensions had not been inclusive.
- The publication of draft clauses is also viewed as an improvement – though has lengthened the timetable to legislation.
- Informal consultation has benefits, but is not a substitute for full, open consultation.

- It is important that consultations are constructed to ensure that interested parties can contribute, recognising that the volume and frequency of consultations could place big demands on those outside the professional tax world to engage, even if they had the inclination to do so.
- There are real resource constraints, both within HMT/HMRC and among consultees. When measures are forced through without adequate consultation, unintended consequences risk being missed, creating problems down the line. Feedback to consultees on responses might improve the quality of engagement.
- A longer timetable for consultations may be helpful, allowing enough time for draft clauses to be considered, and extending the process beyond a year. Officials might need to challenge Ministers more where timetables are unrealistic.
- Longer timetables would be easier if a more strategic approach to tax policy making was taken. If broader consultations on a particular area of tax—for example, property taxation—were undertaken at the beginning of a Parliament, then repeated consultations in successive years on the detail of changes may be reduced.
- Treasury/HMRC might learn from practice elsewhere and in other institutions: for example, New Zealand’s reformed approach to consultation which seeks to engage a broad range of stakeholders – although policy can take longer to make as a result.

*Areas for future focus:*

- How can the transparency of the consultation process be increased, and engagement widened, with inevitably constrained resources?
- How to ensure that consultations are accessible to all those potentially affected?
- How feasible are longer timescales to enable better engagement?

### 3. Internal Budget process

The unique circumstances surrounding the Budget – its status as one of the key political events of the year, the media attention it gathers, and the power of the Chancellor to determine its content — have implications for the way in which tax policy is made, and raise the risks around policy making. The process developed as a way of protecting the Chancellor’s abilities to make tough revenue decisions, but has been maintained as Budgets have expanded beyond taxation, and become major statements of overall political strategy. There are now effectively two major fiscal events a year, as Chancellors see the need (and opportunity) to respond to the OBR’s Autumn forecast which (because of the nine month gap from the March Budget) tends to see bigger revisions to the forecast.

The process has undergone a significant degree of change since the creation in 2010 of the OBR, which provides internal challenge to HMT/HMRC on both the evidence behind individual policy measures and the assumptions behind the costings.

- The Budget is exempted from normal collective decision-making processes applied to other proposals – and the Treasury external challenge that is applied to policies from other departments does not operate when policies are developed within the Treasury.
- The Treasury lead on Budget decisions means other government departments may be consulted on proposals late, or only partially, even where subjects are their lead responsibility. This can create both political and implementation problems, and risks damaging other departments’ relationships with their core stakeholders.
- There is an asymmetry between spending measures – subject to ex-ante challenge by the Treasury, and from the Accounting Officer, and ex-post audit by the National Audit Office – and measures which achieve similar objectives through the tax system. They are also not subject to caps. That risks poorer value for money. These concerns apply to non-tax elements of the Budget and the Autumn Statement as well – and they also apply to announcements made at party conference.
- The perceived political benefits of “Budget rabbits” can lead to poor policy making. Budget secrecy is generally felt to be unnecessary, with a genuine risk of forestalling applying to only a few measures.
- The now near-biannual Budget cycle, with guaranteed Finance Bills, drives the volume of change and the compressed timetable for consultation. There is no external discipline on the amount of tax legislation.
- The Office of Tax Simplification (OTS) has been a positive innovation, but is constrained by both its restricted remit and limited resources.

*Areas for future focus:*

- Is there scope for moving away from an annual (or indeed biannual) Budget cycle and reducing the political incentives for secrecy and surprise announcements?
- How might the length and complexity of Finance Bill legislation be reduced?
- What changes might promote more challenge within the Budget process?
- Is there anything to be learnt from the experience of other jurisdictions’ approach to Budgets?

#### 4. Legislation and legislative scrutiny

The volume of tax legislation is increasing and the quality of scrutiny in Parliament remains poor. The Treasury does not have to bid for Finance Bills in the legislative programme – and Finance Bill legislation is much longer than most other bills (the average length of all bills in 2010-15 was 101 pages).

- There are concerns among practitioners about the increasing volume of tax legislation – HMT produces more legislation than any other department.
- There are also concerns among tax practitioners about the quality of tax legislation itself, including the length of legislation and consistency of terms and definitions used, and the extent to which it accurately translates intent into law. The original Tax Law Rewrite attempt to do “plain English drafting” of legislation has not led to any simplifying of policy.

- The Office of Parliamentary Counsel (OPC) is considered by many to do a good job; but some suggested that the policy intentions of HMT/HMRC are not always accurately translated into legislation.
- One specific problem is the lack of clearly expressed purpose for changes, which makes scrutiny harder. It was pointed out that Ministers are usually very clear in their own minds what the purpose of a measure is, so some way to communicate this better in legislation may be useful.
- In Germany tax legislation is “purposive” in nature. This means that in Germany practitioners do not look for ways around specific drafting, but rather focus on the purpose of parliament. However, this is a very different legal culture and system, which would make it hard to replicate in the UK.
- There are concerns about the quality of information produced alongside tax measures. The quality of Tax Information and Impact Notes (TIINs) is thought to have deteriorated. They should be clear on the cost to business of measures, and should also inform the policy making process rather than be regarded as an add-on at the end. Impact assessments also need to bring out linkages and interactions between the proposed measure and other policies. This would promote better scrutiny. On the other hand, it is felt that equalities impact assessments in TIINs have improved; for example, in the note accompanying 2015 direct recovery of debt legislation.
- HMRC’s Knowledge, Analysis and Intelligence directorate (KAI) has improved the quality of estimation of the dynamic response to Budget measures, but again, while costings documents had improved considerably in 2010, it is felt quality has now dropped back.
- The Commons has shown itself so far relatively reluctant to engage systematically on tax issues, whether through legislative scrutiny or wider work on tax policy. MPs are not very well informed about how the tax system operates – and attempts to offer training have not been successful. Membership of Finance Bill committees also tends to rotate. MPs that speak at all are more likely to focus on challenging or defending government policy rather than ensuring that that policy has been translated into workable legislation.
- The Treasury Select Committee has a wide remit and tends to spend little time on tax. This might be addressed through the creation of a tax-specific committee or subcommittee. The US Congress’s Joint Committee on Taxation might provide a model to draw on the greater tax expertise in the House of Lords.
- Scrutiny of Finance Bills is constrained by a lack of resource and interest amongst MPs. The compressed timetable around Finance Bills limits the scope for proper consideration of many of the clauses in the Bill, and this is compounded by the size of the Bills, driven by the number of fiscal events and degree of fiscal activism.

#### *Area for future focus*

- Would it be desirable to move to consider again more purposive legislation in the UK, or should the focus be on better statements of purpose being provided by government?
- How might TIINs and other Budget documentation better promote scrutiny?
- What might help ministers better communicate the purpose behind tax legislation?
- Is there any scope for improving the capacity of MPs to better scrutinise tax legislation?

## 5. Post-legislative review

The weakness of ex-ante challenge and scrutiny is matched by an absence of external post-legislative scrutiny.

- There is little public systematic evaluation or review of the effectiveness of tax policy measures, and no direct cap on their “cost”. Ministers might be reluctant to see controversial measures reopened.
- One of the roles of OBR is to draw attention to measures where initial cost or yield assumptions have been confounded – for example, the yield from the crackdown on Swiss bank accounts was much less than HMT/HMRC had initially predicted (though practitioners noted they had been sceptical from the start). This acted as an important incentive to improve costing.
- Post-legislative review should focus on whether the measure is raising expected revenue; whether it is achieving its policy objectives; whether it is operating as intended and whether the measure is still needed. This requires clarity upfront about what the measure is intended to achieve.
- There is also little evaluation conducted by academics. More data is being published through HMRC’s Datalab, but data confidentiality means it may not be easy to share this with academics. The degree of change in the tax system also creates barriers to evaluation- either internal or external: by the time that an evaluation has been carried out, the policy may already have been modified.
- When Parliament does engage on tax issues, most scrutiny focuses on new proposals – there is very little capacity or appetite to look at the effectiveness of past measures, or the coherence of the system as a whole. The [Treasury and HMRC challenged the National Audit Office’s](#) right to scrutinise even the most spending-like of reliefs as outside the remit of the NAO Act. If the NAO were to look more systematically at tax measures it would need additional capacity and expertise.
- The OTS is a potential source of greater post-legislative scrutiny, but would need to be resourced to undertake this systematically, and the relationship between doing this and its current function of assessing complexity would have to be thought through. Another option might be to expand the functions of the OBR.

### *Areas for future focus*

- Could TIINs provide a clearer basis for post-legislative scrutiny by setting out what measures were intended to achieve?
- What institutions are best placed to undertake more systematic scrutiny and evaluation? Should this be a role for the NAO, the OTS or the OBR? What role should Parliament play?
- What scope is there for boosting academic evaluations of tax policy?
- Could wider use of sunset clauses force reappraisal of measures – or would this create too much uncertainty?

## 6. Capability

There are concerns about the impact of the 2004 *O'Donnell Review* and the division of labour between HMT and HMRC, particularly the implications this has had for the tax policy making capabilities of each department. HMT is currently working with HMRC to develop a clear public sector tax career path within the departments, which will allow people to progress without having to move to more generalist Treasury jobs, and will encourage more interchange between the departments – but the impact of this initiative will take some time to emerge fully.

- Some officials and practitioners have identified a relative lack of specific tax expertise and experience among Treasury officials who are in the policy divisions. There is a particular concern about the lack of training provided to junior officials who were expected to engage with external experts.
- This is compounded by a perceived lack of institutional memory, in part due to the rapid turnover in staff. It would seem wise to move some staff around regularly (as there is benefit to doing this), but to have some staff who stay working in tax.
- There appears to be reluctance by HMRC officials to see tax policy making as part of their career development – and therefore to seek postings to HMT tax teams. Any lack of engagement of HMRC in policy design risks implementation issues down the line.
- Tax policy making would benefit from hiring more people with high level tax practitioner experience to improve policymakers' understanding of behavioural likely effects and practical impact on taxpayers of proposed changes. Good use has been made of some temporary expert hires on technical issues.
- Secondments are a useful route to bring in external expertise, but secondees tend to be people with 5 years' experience rather than partner level – professional firms cannot offer reverse secondments to HMT/HMRC officials. Parliamentary concern about secondments had had a negative effect.
- Where outward secondments from HMRC have happened, returners found that their experience had not been put to good use on return.
- There is little use of external academic expertise by HMT or HMRC.
- The US Treasury has been able to put senior people into permanent roles (though it was noted that this was a more general feature of senior US government roles) and because this has been done on a permanent basis, not through secondments, fewer questions about conflicts of interest were raised.

### *Areas for future focus*

- How best to support HMT/HMRC's development of a public sector tax policy specialism?
- What would be the best way of training junior HMT/HMRC tax policy professionals? What might be the best way of ensuring they understood potential implementation issues and behavioural responses to tax changes?
- Could barriers to more senior external hires be addressed?
- How to encourage more senior secondments – and make better use of returning secondees?

## 7. Public debate

The *Mirrlees Review* noted the poor level of public debate about tax policy options in the UK, with most generation of options coming from within HMT and HMRC. Other countries have undertaken independent or semi-independent reviews of the tax system, with elements of planned public engagement – and the UK has done this on other difficult long-term policy issues, for example the Turner Review of pensions.

- Many high profile tax commitments are developed for manifestos – and governments are elected with promises to implement them. Some of these commitments are small, stating what the government will do with a specific tax; whilst others are much greater, for example the pensions triple lock. This means that some major options can be cut off before even entering government.
- There is very little public debate in the UK about most specific tax measures, and poor public understanding of key elements of the tax system or the trade-offs policy makers faced. It has to be recognised that many people often want inconsistent things, such as lower taxes with no losers.
- This lack of public debate and understanding distorts government decisions – public debate often focuses on binary questions of tax increases and cuts, or ‘winners and losers’ from the Budget.
- The public also needs to be engaged on operational decisions – for example, the *Making Tax Digital* strategy will affect many taxpayers.
- Schools do virtually nothing to educate pupils on tax issues.
- PwC has experimented with a citizen’s jury approach, which revealed that people make interesting decisions on what they regarded as “fair” taxation when they are exposed to the arguments.
- The quality of many Budget representations is either predictable or poor and driven by special interest groups. The academic community is relatively underengaged in tax policy making – a more vigorous external debate could improve the environment for Budget decisions.
- Making more data available could create a more informed media debate.
- There is a lack of trust – for example on whether businesses paid the right amount of tax – which can erode compliance. There has been a problem with the failure to nip disquiet in the bud – perhaps because of lack of direct Ministerial accountability for HMRC. Better public understanding of the tax system could improve compliance.
- The Turner Review on pensions worked because it had a long time – and was dealing with an issue that required a long-term response.

### *Areas for further focus*

- What might be good ways of fostering better public debate and promoting greater public understanding of the tax system?
- Is there a potential role for intermediary bodies or reviews to play in improving the level of public debate?
- How can greater academic engagement be fostered?