Overcoming barriers to tax reform

Lord Turnbull

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Biographical details

Civil service history

1988–1992: Principal Private Secretary to the Prime Minister (Margaret Thatcher, John Major)

1992–1997: Permanent Secretary, Department of the Environment

1997–1998: Permanent Secretary, Department of the Environment, Transport and the Regions

1998–2002: Permanent Secretary, HM Treasury

2002–2005: Cabinet Secretary and Head of the Home Civil Service

Parliamentary career

2005–present: Crossbench Peer

2015–2019: Member of the House of Lords Economic Affairs Committee and Finance Bill Sub-Committee

Lord Andrew Turnbull was interviewed by Joe Marshall and Thomas Pope on 12 September 2019 for the Institute for Government's tax reform project.

Joe Marshall (JM): Is tax policy uniquely difficult?

Andrew Turnbull: Yes, I think so, because there's a lot of hissing of geese (as Jean-Baptiste Colbert noted). The Budget is, or should be, a strategic statement, but it's not. It has degenerated into a highly tactical event. The chancellor has got to find a little bit of money here and a little bit of money there. You get all these budget starters and, over time, a whole series of decisions and actions take place and you lose the clarity of what it is you're trying to do.

Thomas Pope (TP): You say the budget process has deteriorated, was there a period when it was better?

AT: Well, it was probably better in the Lawson period. Recently, we've had, in effect, two budgets a year, a budget and an autumn statement. This has meant that twice year you've got to play Santa Claus. Now, it's a very good idea to have one budget a year and a kind of updating statement, but that doesn't involve policy announcements.

Government has made some improvements to the budget timetable, so that you get a finance bill published before the start of the year and then there's a chance to debate it now, so the timetable they have improved.

JM: How effective is Parliament's scrutiny of tax policy?

AT: The truth is that Parliament's got the power to scrutinise tax properly, it just doesn't do it. In the Commons, the Finance Bill Committee will go through the finance bill and filter out one or two things and then send it up to the Lords, who don't have the power to modify it. In contrast, for normal bills, the Lords scrutinises the half-done business of the Commons. But it can't do that on the finance bill.

There is a thing called the Finance Bill Subcommittee, but its remit is confined to administration. So, whereas the House of Commons has to arrive at a decision on the finance bill, the House of Lords doesn't, because of Commons financial privilege. The Lords can't apply any degree of scrutiny, so something like the loan charge was nodded through by the Commons, and then all of a sudden people realised there was an issue, a big issue, and that many of the people caught by the loan charge are not there because they decided to go into such schemes, but because their employer told them to. And these are not all particularly wealthy people. Yes, you've got TV presenters and sports personalities and so on, with lots of tax advisers, and they've gone well out of deferred renumeration schemes and they deserve what they get. But there are other cases of people in local government who were told that their contact was ending on Friday, and on Monday they'd be working in a different arrangement. They were told it would be just as good for them, they might even say it'll save you some money, but they had no choice.

HMRC [HM Revenue and Customs] says that it never accepted that these schemes were a way of avoiding tax, so tax was always payable, it just happens that they're asking for it now, so it's not retrospective. But HMRC in many cases has signed off all these people's tax returns, making no attempt to claim this money for I don't know, seven, eight, 10 years. Now, all of a sudden, they are requesting the tax, so it certainly feels retrospective to the taxpayer. And this is something that the Commons didn't spot that at all.

The Lords could also flag administration issues. Take 'Making Tax Digital', this idea that everyone with income, not net income, but income over £10,000 should put in a return digitally in a way the HMRC specifies quarterly. Now, all you young people have got mobile phones. Supposing you're a plumber, you can get all of your receipts on the phone and then it just goes straight into your account and it's all there. But in other cases, it just doesn't work. When the issue turned up in the House of Lords, then we were able to comment on it, because it's about the administration of it, but, by limiting the Lords to administration, you're failing to use a lot of expertise. Take the structure of corporation tax, not taking decisions on whether it should be higher or lower, but the House of Lords could offer some wisdom on its structures. It is prevented from doing so and I think you can allow them to be involved in this process without breaching the views that there is primacy for the House of Commons.

JM: How do you think Lords scrutiny of tax policy could be improved? Is it about changing the remit of existing Lords committees, or joint working with the Commons? With the Treasury Select Committee for instance?

AA: Well, the Treasury Select Committee doesn't look at much tax either. The Lords Finance Subcommittee – which looks at the finance bill - isn't a committee in its own right. All the time it's being told that all it can look at is good administration. You could make that a committee in its own right, but its work would be quite seasonal. Some professional bodies, like the Chartered Institute of Taxation and different representative bodies, would love for the finance bill to be scrutinised to the same degree as any other bill, although providing the Lords the ability to amend anything would run counter to the Parliament Act, and you have to maintain that basic principle.

So, Parliament needs to do better. But now of course bills are all subject to timetable motions, so all those late-night sessions no longer happen, so the scrutiny is much less.

Parliamentary scrutiny is not helped by the lack of a framework on fiscal policy or a taxation framework that outlines what we are trying to do. Those frameworks need to be better articulated, so that each time a measure comes up, you can see how it fits into it. But in practice, a lot of time it is small measures here, small announcements there.

The other thing is that tax reliefs are not scrutinised to the same degree as taxes. If you want to increase a tax exemption, it just slips through more easily. With tax exemptions, you could get a relief that might go from costing £10 billion to £20 billion, and there's not an automatic process where you can ask: why has this happened and what are you going to do about it?

JM: We've heard the review of whether tax reliefs are meeting their objectives is an area where post-implementation review could be improved. Do you think that is an area where the Lords could do more?

AT: Well they could do more. They've got more time. There are too many people in the House of Lords, we've got to give them something to do to earn their crust, as Boris Johnson would put it! Yes, they could look at that because they're not changing the law, but you're getting them to see whether a particular relief served its purpose. There are lots of cases of various business reliefs where you suddenly find that 80% of the income is claimed by a small group. Things do get abused and somebody needs to look out for that. Now the National Audit Office could do more. It doesn't do a lot on tax I don't think.

There is also the Office of Tax Simplification [OTS]. One of the clear limitations is that it acts entirely, ex post. They look at what has happened, and consider whether it was simplest way of doing the policy. They do not get consulted before the policy is made and they do not have the opportunity to say, well if you do that, it's going to make the system more complicated. They need to be a kind of a statutory consultee. So they can consider whether a change is leading to simplification or is it leading to complications? At present, the OTS does worthy work, but it is under used.

The OTS has looked at inheritance tax. The tax is full of complicated rules – such as gifts being tax free if you survive another seven years. This leads on to a question of whether inheritance tax should be recast as a gift tax focused on the amount people receive, rather than on the point of disbursement. Now, I suppose it may be simpler to tax a will, rather than keep track of anything that someone did during their lives. For instance, if I pay for an expensive holiday for the family, is that a gift? Inheritance tax is also full of reliefs, so make sure just before you die you buy a few acres of agricultural land, these things stick around in the system, you know we're not an agriculture economy at all.

But yes, there are ways of getting more scrutiny into the system, but still retain the primacy of the House of Commons and the integrity of the finance bill.

TP: Do you think there's appetite in the Lords for that?

AT: Yes, I think there would be. There are a lot of people who kind of know the tax system, people who have been in business, so there's some quite well-informed people.

JM: Is taking a bigger role in tax something the Lords can do on its own, or does it need a nod of approval from the Commons?

AT: It would need the Commons to say yes. I mean the Commons ought to be prepared to admit that it's struggling. The Commons never expresses any gratitude for the fact that on legislation in general, the House of Lords digs them out of a hole, time and time again. Many of the amendments made to bills at report stage have a 'G' on, they're government amendments, and they come about because, at the committee stage, the minister says "yes well, take it away and think about it and take the Lords advice on board". Sometimes it might be just I'll think about or actually do it, but it's a very valuable function. But that function doesn't happen with the finance bill. And I think the Commons ought to be able to say that, without the Lords usurping our role, we could allow them to get further into tax.

TP: Is your impression that on the Commons side, there's not the expertise or time necessary?

AT: Time as much as anything. They haven't got the time and they choose to use the time they have in other ways. The move to make the hours in the Commons more sociable, has limited the extent to which they can examine things. Now improving the hours is perfectly laudable. But what the Commons hasn't said is that we can't put as much time into scrutiny as we used to, so let's enlist more help from the Lords. The Commons doesn't do that because they all think the Lords is full of old fuddy-duddies in ermine gowns and so on, but they could be more prepared to admit that they struggle with legislation. On the finance bill, in particular, they are not getting anything like the help that they could get.

JM: Do you think the Lords could help provide some political space to talk more sensibly about tax?

AT: It could. There are some issues the Lords would never touch, like rates of income or corporation tax. There's always a debate on the finance bill in the Lords, but it's four hours and you can talk about what you like, but it doesn't lead anywhere really, and it isn't on the basis of a report that a committee has produced. Producing a report on key questions like the proper role of the taxation of housing, would be valuable. There is no way to do it at the moment. It's just too much of a hot potato, no one really wants to do it.

There's also an important difference between select committees and the public bill committee that considers the finance bill. A select committee can call in witnesses and experts. A public bill committee is just the MPs, so if someone like the Chartered Institute of Taxation wants to make representation, they've got to feed into an MP first. I think the finance bill committee should be more like a select committee in the way it gathers evidence.

JM: Do you think the finance bill committee should have a standing membership, as opposed to being appointed ad hoc each time?

AT: Well I think that would help. You'd want to have some kind of rotation and term limit, but yes it would help. I suspect that most finance bill committees, and I've never sat on one, but mostly I think they just comprise of a junior Treasury minister engaged in dialogue with their opposite number of the opposition front branch. The other MPs are just there to vote, I don't think they contribute a great deal.

JM: We have heard the corporate tax road map in 2010 was an example of a clear strategy. Can you think of any other examples when the government has set out a clear approach to tax policy?

AT: Well, you could say the Dilnot review into long-term care (and other reviews on this topic before Dilnot) was an attempt to set out a long-term strategy. It wasn't really on tax, but it had many of the same features, it was basically asking how is this expenditure going to be funded? It needs to be a joint thing where the government pays some of the cost and the families also pay some (and then there are different views on whether the government share is paid for by central government or local government).

Where the reform of social care has gone wrong is that no one has been prepared to confront the public with the fact that we cannot afford to provide social care on the NHS basis, free at the point of need, because the amount of need would just explode and it would become more expensive than they ever thought it was going to be, as indeed it did with health. It would also raise questions about why really wealthy people should get health treatment on exactly the same basis as people that have got no money at all. Therefore, there must be some, family contribution.

Now, the only example I can think of successful long-term reform is the increase in pension age. There was a long debate about raising the pension age. People didn't like having the pension age raised, most of all women because they had to get from 60 up to 67 and the men only had to go up from 65 to 67. But, in the end, after a long debate, people kind of recognised that it had to be done and the pensions commission contributed to this.

In taxes, a lot of these difficult decisions are dodged and too much of tax policy is very, very short term. Suddenly we're going to raise the threshold or change rates. It might be a good thing to do, but there are consequences in terms of working out how they are going to be funded and what that means for the rest of the system.

So, you need to lay out some plans. On the road map for corporate tax, you have to ask why do you think it's important to get down to below 20? Apart from Ireland, very few countries have really gone that far.

The other road map that's needed is on merging national insurance and income tax. On national insurance, the amount of money you pay in bears no relation to what you get out, that's long since gone. The only thing that happens is that the number of occasions of which you've paid in money, over what period, does determine eligibility, to some extent. Having both taxes creates lots of distortions, but merging the administration would also be difficult, what happens to gift aid, for example.

When you have major tax reform, some people are going to benefit, and some people are going to lose. So, you've got to be prepared. You need to have enough money available so that you can minimise the losers. And this hasn't been available. While we're in a period of austerity, wholesale reforms are much more difficult because you can't buy out the losers very easily. Maybe we'll get back to a time when it gets easier, but it's not just around the corner.

JM: If governments are willing to spend that money, how do you convince governments to spend that money on big structural tax reforms rather than funding public services or doing other things that are popular?

AT: Well, it seems to me that what we're trying to do is run public services on a kind of north European level on tax rates that are much lower, probably 10% of GDP [gross domestic product] lower. You can see that some quite important services are really creaking at the moment, the justice system, where legal aid has got to, is pretty mean at the moment, long-term care severely underfunded, schools, pretty poorly funded, and gradually the government is trying to build some of that funding back, but it still has its views that it wants to cut taxes. Really taxes need to go up in my view.

If you get to a point where debt as a proportion of GDP is rising, you're not in a sustainable fiscal position. Once you get in a position where you are borrowing, but the borrowing is such that the debt-to-GDP ratio is falling, which is around 3% of GDP something like that, you can borrow 3% GDP and the debt ratio will not go up. As long as the economy is growing – and a recent lack of economic growth is also part of the problem.

I also think that concern about government debt is exaggerated. Debt-to-GDP is now, let's say 80%, it used to be 40%, but debt interest to GDP is exactly the same – around 2.5% – as it was in 2008 and interest rates have come down.

In a survey people will agree to putting up taxes to pay for better public services, but in practice it never makes you popular, and which is why increasing the tax take is easier when the economy is growing, because you don't have to put taxes up, or you just allow fiscal drag to do the work.

Taxation is invertebrate, there are no bones to it, there's no shape to it, and you need some bones to scrap the basic shape, and no one wants to talk about the skeleton of the tax system.

TP: Did you have any idea about how a skeleton for the tax system could be put together?

AT: Well, at times people have talked bravely about it. Under Gordon Brown, Nick Stern was supposed to think about the tax system, but Brown, about six weeks into it, decided he wasn't interested in Nick Stern's great ideas, he kind of, lost interest in him and Nick went off to do other things.

But at the moment there is just a sense of drift and budgets are a series of initiatives where chancellors say, "oh we're spending £200 million more on this". It's a very common failing of the civil service actually, using those figures. How big is £200 million? Is it big in relation to what they're spending now, what we were spending last year, what the need is, what the impact is? You just get a number and that allows anyone going on the *Today Programme* to say yes, but we've added another £300 million to the schools budget. Is £300 million material? Gordon Brown used to say "we're going to spend a billion pounds over five years", what he meant was he was spending £200 million a year. So, there needs to be clarity over numbers and less of a reliance on apparently impressing people with little dollops of money here and there, which don't do very much.

JM: Do you think putting numbers into context would help improve public understanding of public finances?

AT: Yes. There have been various attempts to outline government spending. For instance, when you get your tax notice that tells you how your tax is spent, that is better than nothing.

But it's difficult, if you simply take government debt, that's a very, very poor measure, because it doesn't include the assets that that are created with that debt (it's not measuring net wealth). It also doesn't address the fact that spending money on the health service is a commitment just as binding as a gilts. The OBR [Office for Budget Responsibility] does produce reports looking into these sorts of figures, but it never really gets picked up.

We're locked into a very simple argument that we've got to get borrowing down because we can't pass the burden to future generations. But if most of the borrowing is borrowing from one lot of citizens to another lot of citizens, the country is not impoverished by that, because someone's got an asset and someone's got a liability. But if you are spending a lot of money on public services, and spending on the health service is described as an investment, it's not an investment at all, it's a cost. So, getting some rigour into the language that we talk about tax and spending is essential.

TP: Shortly after your time at the Treasury, the O'Donnell review proposed merging the Inland Revenue and Customs departments and moving the tax policy function into Treasury. Did you recognise the weaknesses the O'Donnell review identified and agree with the solutions proposed?

AT: I think it was probably an improvement. There was pretty good dialogue between the Revenue departments and the Treasury. The Inland Revenue guys in Somerset House did most of the finance bill work.

But if tax policies are produced in a very opportunistic way and are highly politicised, the benefits you get from the reforms are not really going to be garnered, I don't think. But it was a reasonable thing to do, I think having the tax experts literally at one end of the same building creates the potential for the system to work better. It doesn't necessarily mean it is working better, but it could work better.

TP: Do you think communication between those doing tax policy and the tax administration is key?

AT: Well, the communication and then the thinking about the application of technology.

JM: Can you give an example where the application of technology was not successful?

AT: I think tax credits ran into problems almost for cultural reasons. Inland Revenue, from its inception, collected money from big companies on their corporation tax and used the big companies or employers to collect the money on your pay. They didn't actually care where you lived, it was completely irrelevant to them, and they didn't actually want to deal with you at all. So, they wanted to have a PAYE [pay as you earn] system that got it right, so they taxed you on income at source, and banks paid you net, dividends were net and so basically, the system sorted it out, you didn't need to deal with people.

All of a sudden with tax credits, you're dealing with, let's say, the bottom 20% in society, the poorest 20%, who often live pretty rackety lives actually. They scratch around for income wherever they can get it, they don't keep many records, and their circumstances change rapidly. In contrast, everyone in HMRC are graduates, they've all got long-term contracts, they're all paid monthly, and they all learned to budget and live their lives on that basis. When you start out with something like tax credit, you're trying to apply to a culture where everyone is paid weekly, and sometimes they go for some weeks where they get a lot of money and another week where they get no money at all. You've got all sorts of families, single parents, it's tremendously complicated and I just don't think the people in HMRC, when they designed these schemes, had any sense of how people are forced to live their lives.

For example, the social security system, when paying benefits, for accommodation they would take the money, the housing money, the rent money and deduct it from the benefit, and then they would pay the rent money to the landlord. Universal credit says no, no, no, you're grown up people here, we give you the money and you pay the landlord. Now, the effect of this is that the landlords suddenly think, my tenants aren't nearly as good credit as they were. People are being evicted, not because they're really in arrears, but just because, if they were to get into arrears, it's going to be difficult to sort it out. So, in designing these systems, government doesn't make enough allowance for just how difficult and precarious many people's financial circumstances are. So, I think that's where they're struggling.

JM: Given your reflections on tax reform, what advice would you give to your successors in the Treasury to help them support the government to successfully reform the tax system?

AT: Well, I think you've got to think in terms of road maps, ask where is the system going? Before you get down to the list of individual measures, I think more work needs to be done on thinking about where you want the system to be in five years' time, not just in how it's administered and so on, and not just on specific issues like the tax gap. Now, that strategic thinking should include threats to the tax base, for instance the digital economy is decimating the high street. But technology has also got big potential to help generate revenue. Dematerialising transactions and taking them off shore is also a problem, but there will be opposition from big tech firms. The OECD [Organisation for Economic Co-operation and Development] is doing work about this. I think it's a case of being brave and saying we're going to introduce a kind of deemed income tax and then other countries will follow. The French are planning to act, and we ought to be backing them up and say yeah if you do it, we'll follow you into this space.

The changing structure of employment is also a problem in a world where people have lots of jobs. I've never thought a local income tax is the answer. You could tax people on the basis of where they live, where their employer is, where they actually do the work, and where the transaction actually takes place. Now, they're all different, so you could live in Carlisle, work for an accountancy firm in Edinburgh, but actually serve clients both sides of the border. Now, who's got the right to the income that you generate? Scotland is a very interesting. There is a geographical thing about Scotland, there's a kind of demilitarised zone, you draw a line from Carlisle to Newcastle, then there's 100 miles north of that there's little apart from sheep, that makes separating out what goes to Scottish taxation much easier than someone on the Welsh border where, what's the difference between Chester and Wrexham?

The gig economy is going to be much more difficult to tax, you know the PAYE system is incredibly efficient when large numbers of people come together with a single employer in a single facility. But the PAYE system will become less and less effective over time, and then you've got to find other ways of collecting tax, which is maybe why you should probably try to get more out of VAT. But VAT has its own problems. So, you have to ask what is threatening your current tax base? And at the moment you know it is kind of all hands to the pump, just surviving really.

TP And do you think that long-term horizon scanning is something that the civil servants can be doing, even if that's not kind of the focus of ministers?

AT Well, I think that civil servants should be doing it really, with input from special advisers. There ought to be a kind of triangle relationship in policy making, you've got ministers, special advisers and the officials, and they should all work together, and they should communicate with each other. It goes wrong when special advisers try to stand between the ministers and the officials.

The whole policy process can be seen as a circle, you start off with what’s happening on the ground, and collecting data on it, and then someone has to analyse that data to see if we getting as much revenue as we thought and if it’s working. And then you've got to say whether you’re satisfied with that or not, and what are you going to do about it? And the bit that special advisers like is the bit where you come up with ideas, like, let’s get housing associations to offer a right to buy, I guess that sounds like a good idea, okay. But once you've got this, you’ve got to consult about it and then you’ve got to legislate for it, and then you’ve got to design a delivery mechanism for it, then you’ve got to start collecting the data on what effect it’s having and you go round in a circle again. On a clock face, special advisers work at somewhere between 2 o’clock and 3 o’clock, clever ideas men. Are they interested in the consultation bits? No, they want to give a quick decision. Are they interested in analysing the data? No, that’s too boring. So, you need someone who can provide and challenge ideas and so forth, but they've got to be prepared to do the hard work in the rest of the cycle. At the moment, I think the civil service has been pushed aside, and the special advisers, particularly in and around Number 10, are too powerful. Special advisers are valuable, because they keep up the pressure to say you’ve got to think differently, but you’ve still got to allow all the other aspects of good policy making to come into play.

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