



HM TREASURY



HM Revenue  
& Customs

# Tax policy making: a new approach

June 2010





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# Foreword

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Making the right decisions on tax policy is critical – it makes a difference to almost every business and citizen in the UK. This is more important than ever, as we face the urgent task of reducing government borrowing. As the Minister with overall responsibility for the UK tax system, this responsibility is at the forefront of my mind.

The Government is committed to creating the best possible environment for a private sector led economic recovery. A competitive tax system is at the heart of our approach, and the Budget sets out a significant package of reforms to the corporate tax system. But a competitive tax system is not only about the level of taxation and the policy choices that determine its incidence. It is also about the quality of our tax law and the way in which we make tax policy. How we:

- propose;
- consult;
- legislate;
- implement; and
- evaluate changes to the tax system.

I am frequently told by businesses and the tax profession about the importance of predictability, stability and simplicity in the tax system. Business and tax professionals have previously criticised the tax policy making process as piecemeal and reactive, pointing to the wide range of policy announcements in recent years that have been unexpected and insufficiently thought through.

I want a new approach to tax policy making; a more considered approach. Consultation on policy design and scrutiny of draft legislative proposals should be the cornerstones of this approach. The Government will always need to maintain flexibility to make changes to the tax system. But in doing so, it should be transparent about its objectives, and open to scrutiny on its proposals.

The issue of tax policy making is high on the agenda of tax professional bodies and many business representatives. There have been many reports written by well-respected experts in this field, but with little comment from government to date. As a Government, we share the objectives of business and the tax profession to have a more deliberative process in making tax law, with legislation of the highest quality. I hope that this discussion document will provide a platform for the Government to engage with interested parties over the summer, to help shape a new approach to tax policy making.



David Gauke MP

Exchequer Secretary to the Treasury





# 1

## Introduction

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**1.1** As set out in the Coalition Programme for Government, the tax system needs to be reformed to make it more competitive, simpler, greener and fairer. The Government wants to ensure that the tax system better reflects its values and priorities. For example, major tax reform is necessary to restore competitiveness of the UK economy. This will, in part, be achieved through the reforms to the corporate tax regime set out in the Budget

**1.2** In addition to structural reform, it also requires reforms to the way tax policy is made to restore the UK tax system's reputation for predictability, stability and simplicity. Better tax policy making needs to be underpinned by greater transparency, a central theme in the Coalition Programme for Government. The Government understands the value that taxpayers place on these objectives and will make them central to its approach to tax policy during this Parliament.

### Case for change

**1.3** Business and tax professionals have consistently pointed to the way in which tax policy is developed, legislated and implemented as a contributing factor to overall complexity and uncertainty. The concerns they have identified with the current system include:

- a lack of clear strategy for the tax system;
- consulting too late in the policy development cycle;
- length and complexity of the tax code;
- uncertainty due to the volume and timing of tax changes; and
- inadequate Parliamentary scrutiny of tax legislation.

**1.4** In July 2008, a Working Party chaired by Lord Howe of Aberavon published a report taking forward the Forsyth Tax Reform Commission's recommendations on the making of tax law<sup>1</sup>. The report identified a series of tax policy reforms that had served to undermine the reputation of the UK as a stable tax environment – not only due to the policies themselves, but also the way in which the policies were announced and implemented. It recommended a number of reforms to the framework for making tax law.

### A new approach

**1.5** Building on those recommendations, the Government is committed to a new approach to tax policy making, designed to support its ambition for a more predictable, stable and simple tax system:

- **to increase predictability**, the Government will provide taxpayers with clarity on its approach and certainty on the future direction of the tax system;
- **to increase stability**, the Government will slow down the rate of change to the tax code, focusing on fewer and better developed proposals supported by improved processes for changing tax law; and

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<sup>1</sup> Making Taxes Simpler. The final report of a Working Party chaired by Lord Howe of Aberavon, July 2008.

- **to increase simplicity**, the Government has confirmed its intention to create an independent Office of Tax Simplification.

**1.6** It is also important that the Government is held to account in the development of tax policy:

- when the Government makes changes to the tax code, it will ensure there is sufficient opportunity for policy and legislation to be properly **scrutinised**;
- to support good scrutiny, the Government will be more **transparent** about the rationale and impact of tax policy changes; and
- to maintain integrity of the tax code, the Government will **evaluate** the impact of significant changes after implementation.

**1.7** To underpin these commitments, this discussion document sets out a number of proposals for improving the framework for developing, legislating and implementing tax policy. Over the summer, the Government will meet with interested parties to discuss its overall approach. In addition, there are a number of specific areas (summarised in Chapter 4) where the Government will have more detailed discussions to help develop its thinking.

**1.8** If you have any comments on the proposals set out in this paper please email [taxpolicymaking@hmtreasury.gsi.gov.uk](mailto:taxpolicymaking@hmtreasury.gsi.gov.uk) by 22 September 2010. If you wish to be involved in discussions on this new approach or have a specific interest in a particular proposal please email [taxpolicymaking@hmtreasury.gsi.gov.uk](mailto:taxpolicymaking@hmtreasury.gsi.gov.uk) by 12 July 2010.<sup>2</sup>

**1.9** Cerys Morgan (Budget Strategy and Tax, HM Treasury) and Cheryl Scott (Central Policy, HM Revenue and Customs) will lead this work over the summer and can be contacted via the email address above.

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<sup>2</sup> Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004. If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Treasury and HM Revenue and Customs (HMRC). HM Treasury and HMRC will process your personal data in accordance with the DPA and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties.

# 2

## Predictability, stability and simplicity for the UK tax system

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2.1 The Government is committed to restoring the UK tax system's reputation for predictability, stability and simplicity. The Government will always need to preserve its ability to respond quickly to particular circumstances through changes to the tax system. However, preserving flexibility does not preclude a new approach to tax policy making that:

- establishes greater discipline on policy makers;
- provides greater certainty for taxpayers on the timing and process for announcing tax policy changes; and
- creates an impetus for simplification of the tax system.

2.2 This requires genuine reform to the framework for tax policy making. This chapter sets out a wide range of proposals that will change the way that tax policy is developed and legislated.

### Predictability

2.3 The Government recognises the value that businesses attach to predictability. It is committed to providing clarity and certainty on the future direction of tax policy. **When embarking on significant areas of reform, the Government will set out:**

- its policy objectives;
- how the reforms will be taken forward, including the approach to consultation; and
- the proposed timetable for reform.

2.4 The Government is applying this approach to the major reform of the corporate tax regime set out in the Budget.

### Stability

2.5 The Government wants to restore the tax system's reputation for stability. It is committed to making fewer piecemeal changes to the tax code and to slowing down the rate of change. When the Government does introduce changes, it will do so in a more considered way.

### Consultation on tax policy

2.6 The Government recognises the value that policymakers and taxpayers derive from effective consultation. It is an integral feature of all policy making. It helps ensure that changes are well targeted and without unintended consequences, and that legislation is right first time. There has been greater consultation on tax policy in recent years, and some notable examples of best practice such as the review of HMRC's powers. The Government is committed to ensuring that all tax consultations are conducted to a high standard. **The Government will publish a statement on its approach to tax consultation later this year. It welcomes discussion with interested parties on the scope and content of that statement, including the proposals set out below and other improvements that could be made to the current approach.**

**2.7** There are three stages to the development of tax policy:

- stage 1 – set out objectives and identify options;
- stage 2 – determine the best option and develop a framework for implementation, including detailed policy design; and
- stage 3 – draft legislation to effect the proposed change.

**2.8** The Government has identified a number of improvements that could be made to the current consultation process, including:

- consulting at each identifiable stage for all tax changes, where proportionate and practical to do so, and where revenue is not put at risk. For the simplest tax changes these three stages may run together, but for major reforms each stage will be distinct and may run for many weeks or months;
- where the Government does not consult at a particular stage, explaining why;
- always setting out at what stage in the policy cycle the consultation is taking place, so that respondents have a clear remit and expectation;
- ensuring that consultations clearly set out the policy objectives, impact analysis, and assumptions on which the policy has been developed; and
- setting out who is leading on each individual consultation and the strategy for stakeholder engagement.

**2.9** The Government welcomes views on this approach.

### **Consultation on tax legislation**

**2.10** The Government is committed to providing taxpayers with more clarity and certainty in its approach to tax policy. **It welcomes views on a new convention, akin to that put forward in Lord Howe's report, that the majority of changes to tax law are:**

- **confirmed no later than three months before the tax year in which they come into effect or publication of the Finance Bill in which they are to be included; and**
- **accompanied by draft primary legislation and, where appropriate, significant statutory instruments.**

**2.11** The objectives of this proposed convention are two-fold. Firstly, it would provide a dedicated window for pre-legislative scrutiny, demonstrably improving the quality of tax legislation. Secondly, it provides greater certainty to taxpayers in relation to forthcoming changes ahead of the tax year. In practice, this would result in the vast majority of the Finance Bill being published, in draft, three months before formal publication. However, there would be some exceptions. For example:

- straightforward changes to rates, allowances and thresholds;
- revenue protection measures; and
- areas where forestalling presents a significant risk.

**2.12** This would be a significant change. Combined with a strong commitment to consultation, the convention will require a longer and more considered policy cycle for changes to tax legislation. This, in turn, will result in a more stable tax system. It will also provide external interest groups and Parliament an opportunity to scrutinise the draft legislation before formal Parliamentary processes commence.

**2.13** The Government welcomes views on this approach and in particular on when business and tax professionals would find it most useful for draft legislation to be published. For example, the Government has received some representations that the objectives may be better met by publishing more background on the policy proposal, including objectives, with draft legislation published a few weeks later.

### **A strategic approach to tax avoidance**

**2.14** The Government is committed to tackling tax avoidance and will continue to take necessary steps to protect the Exchequer and maintain fairness in the tax system. The rules on disclosure of tax avoidance schemes have made it possible to move quickly to close off avoidance opportunities by making changes to legislation. However, the way in which tax avoidance has sometimes been tackled has contributed to instability and complexity:

- frequent announcements of legislative change contribute to the perception of instability in the tax system; and
- detailed anti-avoidance rules have contributed significantly to the complexity of the tax code.

**2.15** The Government will take a more strategic approach to the risk of avoidance to prevent increasing complexity and reduce the need for frequent legislative change. Its approach will be to:

- build in sustainable defences against avoidance opportunities when undertaking policy reform, for example, through legislative approaches that clearly set out the intended objectives;
- review areas of the tax system in which repeated changes have been necessary to close loopholes and seek to strengthen the legislative framework;
- consider, against the background of developing more sustainable defences, whether a General Anti Avoidance Rule (GAAR) should form one element of strengthened defences. Recognising the range of views on the implications of a GAAR, HMRC will engage informally with interested parties over the summer to explore whether there is a case for developing a UK GAAR, taking into account other planned changes, such as corporate tax reform; and
- look critically at the need to announce legislative changes taking immediate effect outside fiscal events and develop a clear protocol for the circumstances in which the Government would be willing to make such announcements. It will work with interested parties in developing this protocol.

### **Common commencement and announcement dates**

**2.16** The previous Government introduced common commencement dates for most business regulation, but these have not generally applied to tax. While many tax changes are announced at set fiscal events and are effective from the start of the tax or financial year, **the Government is interested in views on whether there is a case for further rationalisation of the dates on which tax changes are announced and come into effect (for example, statutory instruments)**. The objective would be to bring greater discipline to tax policy making, improve overall management of changes to the tax code, simplify compliance with the tax code and provide business with greater certainty. The Government recognises that the approach would need to be designed specifically for tax, and may vary across the main taxes.

**2.17** Over the summer, the Government will discuss this with interested groups. If there is a good case for change, the Government will bring forward detailed proposals for wider consultation.

## Simplicity

**2.18** The UK tax system is complex. The Government is committed to a simpler tax system. In the Budget, **the Government has confirmed its intention to create an independent Office of Tax Simplification**. Further details will be announced shortly.

**2.19** In designing new tax policy, the Government will give weight to simplicity, alongside other policy objectives. This will ensure that, as far as possible, reforms minimise transitional costs on business and the burden of complying with the tax system.

### Reliefs in the tax system

**2.20** The creation of reliefs or exceptions in the tax system can add to complexity. Consistent with the broader regulatory reform agenda, the Government will consider proposals for new reliefs carefully, and will want to satisfy itself that there is a strong and proven case. To help inform these decisions, **the Government will develop a framework for the introduction of new reliefs**. It also proposes to make greater use of sunset clauses and post implementation evaluation, to ensure that the case for continuation of the relief remains strong.

# 3

## Increased accountability for tax policy

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**3.1** The Government is committed to increasing confidence in tax policy making. When the Government makes changes to the tax code it is vital that there is sufficient opportunity for the policy and legislation to be properly scrutinised. More effective scrutiny requires greater levels of transparency about the rationale and impact of tax policy changes. Scrutiny should not be restricted to the period just prior to implementation. To be more effective, it also requires greater evaluation of tax policies after they have been in operation.

### Greater scrutiny for tax policy and legislation

**3.2** Making the right decisions on tax policy is critical – it affects almost every business and citizen in the UK. Getting the legislation right is equally as important, both to ensure that the policy is implemented in the most effective way, but also to ensure that taxpayers have certainty about how the changes apply to them. The Government is committed to consultation – providing an important opportunity for interested parties to help shape tax policy and scrutinise legislation.

### Scrutinising draft legislation

**3.3** As set out in Chapter 2, the Government is considering a new convention for tax policy. This will involve confirming the majority of measures that will be included in the following Finance Bill at least three months before formal publication. Subject to views on this proposal, to enable effective scrutiny, the confirmation will be accompanied by:

- draft legislation for inclusion in the Finance Bill;
- accompanying Explanatory Note; and
- a technical note, where appropriate, setting out how the legislation is expected to work in practice.

**3.4** Subject to views from interested parties, the Government proposes a minimum of eight weeks for comments on the draft Finance Bill legislation. This will ensure that there is sufficient time for the Office of Parliamentary Counsel to consider comments and amend the draft legislation, where necessary, ahead of publication of the Finance Bill.

**3.5** However, a significant volume of changes to the tax code are dealt with outside the Finance Bill, through secondary legislation. **Where secondary legislation makes a substantive change to the tax code, the Government will apply the same principles and disciplines as are applied to Finance Bill legislation**, including publishing the legislation in draft for scrutiny. For secondary legislation, the Government proposes a minimum of four weeks for consultation on the legislation itself.

**3.6** The Government welcomes views from interested parties on the practicalities for consulting on draft legislation, including the format and channel for providing comments, to ensure that it is efficient and effective for all involved.

### Role of the Office for Budget Responsibility in scrutinising costing of tax policies

**3.7** The Office for Budget Responsibility (OBR) was formed in May 2010 to make an independent assessment of the public finances and the economy. It is being chaired, on an

interim basis, by Sir Alan Budd. The interim OBR has been given direct control over the forecast for the public finances and make all the key judgments that drive it.

**3.8** The interim OBR has scrutinised the costings of tax policy measures announced in the Budget that affect the economy and public finance forecasts. Continuing to base policy decisions on a realistic assessment of the public finances and having the fiscal impact of tax policy measures scrutinised by the OBR will improve the quality of tax policy making.

### Role of Parliament

**3.9** Tax legislation is currently drafted to a much shorter timescale and with less Parliamentary scrutiny than is the case for most other Bills across Government. This is despite the fact that tax legislation provides for the collection of vital revenues and impacts on just about every business and individual in the country. Tax legislation is regularly challenged in the Courts, where Parliament's intentions as set out in Finance Acts are considered.

**3.10** A wide range of bodies and individuals have looked at the role of Parliament in the making of tax law. There is a common consensus that Parliament should have a stronger and more effective role in scrutinising tax legislation. This requires changes to the way in which Parliament scrutinises tax policy and legislation.

**3.11** The Government is taking significant steps to facilitate greater scrutiny of tax legislation, for example its commitment to publish a significant proportion of the Finance Bill in draft at least three months before formal publication. **The Government will welcome any consideration by the Treasury Committee of how Parliament's role could be strengthened in relation to scrutiny of tax legislation.**

### Effective scrutiny requires greater transparency

**3.12** To support effective scrutiny of tax policy and legislation, the Government is committed to greater transparency. As a general principle, the Government will provide more information on the underlying rationale for tax policy changes, accompanied by supporting analysis and assumptions. It is also proposing a number of changes, to underpin this new approach.

### Improving impact analysis

**3.13** The Government is committed to fully understanding the wide range of impacts associated with tax policy options to inform decision making. **It will introduce a tailored Tax Impact Assessment, in place of the current regulatory Impact Assessment used elsewhere in Government.** It will cover a wider range of impacts than the current approach. Officials from HM Treasury, HMRC and Business, Innovation and Skills will work with interested parties over the summer to develop a new model.

### Publishing more detail on costings of tax policy

**3.14** To improve transparency and scrutiny **the Government is committed to publishing more information on tax policy costings.** Alongside the Budget, the Government is publishing *Policy costing methodology*. This document explains the general methodology used to calculate the cost or yield of each government policy shown in Table 2.1 of the Budget document. It also includes more information on the methodology and assumptions underlying the costings of key tax policies in this Budget.

### Improving supporting documentation

**3.15** The Government is also committed to improving and rationalising the wide range of supporting documents that accompany tax changes without compromising the level of information provided to interested parties. In doing so it will look at approaches taken in other countries, including New Zealand, Australia and the USA.



## Evaluating tax policy

**3.16** As well as providing for more scrutiny of tax policy changes, the Government also recognises the importance of evaluating the impact and effectiveness of tax policy reforms after they have been implemented. Evaluation is an important feature in any policy making process; and particularly in tax given its breadth of impact.

**3.17** The Government is committed to evaluating the effectiveness of tax reforms, to ensure that they are meeting their objectives. To embed this discipline in tax policy making, consistent with the broader regulatory reform agenda, **the Government will consider greater use of sunset clauses or a trigger for an evaluation in legislation.** It will ensure that evaluation is conducted in a transparent manner, and where appropriate, policies or reliefs that are not meeting the original objective will be reviewed.



# 4

## Next steps

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**4.1** In this discussion document, the Government has set out a new approach to tax policy making. The Government welcomes feedback from interested parties on the overall approach, and on the specific proposals that underpin this new approach.

### Summary of proposals

#### To promote greater predictability, the Government will

- set out its objectives for major areas of reform, how the reforms will be taken forward and the timetable.

#### To promote greater stability, the Government will:

- publish a statement on its approach to consultation;
- consider a new convention to confirm the majority of tax changes at least three months prior to the start of the tax year they come into effect or publication of the Finance Bill in which they will be included;
- take a more strategic approach to tax avoidance and develop a protocol for announcements taking immediate effect outside fiscal events; and
- re-examine the case, and scope, for common commencement and announcement dates in the tax system.

#### To promote simplicity, the Government will:

- create an independent Office of Tax Simplification, with further details announced shortly; and
- develop a framework for the introduction of new reliefs.

#### To provide for greater scrutiny, the Government will:

- publish more tax legislation in draft, to allow for pre-legislative scrutiny; and
- welcome any consideration by the Treasury Committee to review how to strengthen the role of Parliament in scrutinising tax legislation.

#### To support transparency, the Government will:

- introduce a tailored Tax Impact Assessment, replacing the current regulatory Impact Assessment used across Government;
- publish more information on costing of tax policies;
- improve supporting documentation accompanying tax changes; and
- consider greater use of sunset clauses for post implementation evaluation.

## Questions for discussion with interested parties over the summer

**4.2** Over the summer, the Government will meet with interested parties to discuss the new approach outlined in this document and some of the substantive proposals that it has set out. In particular, the Government welcomes views on:

- the overall approach and whether the proposals identified will address some of the shortfalls of the current system;
- the proposal for a new convention for confirming tax changes at least three months before the start of the tax year, or publication of the Finance Bill in which they are to be included, and at what point to publish draft legislation; and
- whether there is a strong case for applying the principle of common commencement and announcement dates to parts of the tax system.

**4.3** The Government will work with interested parties on the following specific areas:

- a statement on its approach to consultation;
- a protocol for tax announcements that have immediate effect outside fiscal events;
- the case for developing a General Anti Avoidance Rule;
- developing a Tax Impact Assessment; and
- improving supporting documentation accompanying tax changes.

## Working with interested parties to develop and oversee this new approach

**4.4** As part of the implementation of this new approach, the Government will establish a forum of tax professionals who will meet bi-annually with Treasury Ministers. The making of tax policy will be a standing agenda item. The Government will initially use this forum to:

- discuss the overall approach set out in this discussion document; and
- drive forward implementation.

**4.5** However, it will also expect the forum to challenge the Government if the new approach set out in this discussion document is not being followed or is not having a demonstrable effect on the predictability, stability and simplicity of the UK tax system.

**4.6** If you have any comments on the proposals set out in this paper please email [taxpolicymaking@hmtreasury.gsi.gov.uk](mailto:taxpolicymaking@hmtreasury.gsi.gov.uk) by 22 September 2010. If you wish to be involved in discussions on this new approach or have a specific interest in a particular proposal please email [taxpolicymaking@hmtreasury.gsi.gov.uk](mailto:taxpolicymaking@hmtreasury.gsi.gov.uk) by 12 July 2010.<sup>1</sup>

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