



HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ

**Rt Hon Michael Jack, Chairman
& John Whiting, Tax Director
Office of Tax Simplification
1 Horse Guards Road
London SW1A 2HQ**

19 March 2014

Dear Michael and John,

UPDATE ON OFFICE OF TAX SIMPLIFICATION REVIEWS

As you know, the Chancellor made several announcements in the Budget related to the work of the Office of Tax Simplification (OTS). I am writing to thank you and your colleagues for your input to this process and for your excellent recent reports on the taxation of partnerships, and employee benefits and expenses. I would also like to update you on the government's progress in implementing your recommendations from these and earlier reports.

NICs for the self-employed

Following consultation last summer, HMRC will simplify NICs for the self-employed by collecting class 2 through Self Assessment from April 2016. Implementing this recommendation from your small business tax review will abolish an entire NICs collection process for up to around 5 million people.



The starting rate of savings income tax

You will have seen that Budget announced reforms to the starting rate of income tax, to be implemented in April 2015. These reforms will mean that over 1 million people will no longer need to contact HMRC to reclaim tax through the R40 process, but can instead fill in an R85 form online or in branch at their bank. Whilst a minority of gainers will still need to use the R40 process, the increased generosity of the starting rate (in terms of the size of the band and the zero rate of tax) means we expect a greater proportion of those eligible, to reclaim their tax. Your Pensioners Review recommended abolishing the 10p starting rate of income tax in April 2015. We took a slightly different approach but the reforms achieve many of the OTS' objectives without generating losers.

Review of partnerships taxation, interim report

I welcome your interim report, and I am grateful to you for helping to simplify this multifaceted area of the tax code. In response to your report, HMRC will publish a draft consolidated "Partnership Tax Manual" for external comment in April 2014. This will make it easier for businesses to access guidance for partnerships in one place. HMRC is also working with the department of Business Innovation and Skills (BIS) to re-publish the model partnership agreement, and believes that this can be integrated within the consolidated guidance. Your interim report highlights areas where guidance can be



improved, and HMRC will make changes to address these by the end of 2014.

HMRC will also complete further work to explore the feasibility and cost of making your recommended changes to the partnership and corporation tax returns, and to the process for issuing UTR's. HMRC will report back on these before the end of 2014. A full response to the 'short-term fixes' is set out in an annex to this letter. I look forward to considering any further work you do on the areas you identified as priorities for longer term consideration.

Review of employee benefits and expenses

Further to our last meeting, I am pleased to report that HMRC will take forward almost all of your recommendations, as outlined in your final report on employee benefits and expenses. In particular the Government will be consulting on the introduction of a framework to allow voluntary payrolling of benefits by employers. Your report also identified many problems with the tax treatment of travel and subsistence expenses caused by more fundamental concerns, so the government will undertake a wider review of these. The Government recognises both the complexities you highlight in the report, and the need to reform policy to reflect our 21st century workplace and labour market, so it will also call for evidence on modern remuneration practices to inform future policy in this area. The Government's response to the 'short-term fixes' are set out in full in an annex to this letter.



I am pleased to confirm that of the 43 'quick wins' recommended in the OTS interim report, all nine scheduled for completion by January 2014 have been delivered. A further ten quick wins will be implemented in this Parliament.

Employee share schemes

Finance Bill 2014 legislates for five recommendations made in your report on unapproved share schemes, as well as earlier recommendations for self certification by companies of tax advantaged employee share schemes; online filing of tax advantaged employee share scheme forms; and more clarity around features that are not permitted within these schemes. Your recommendations are enabling us to undertake the most significant package of reform to the tax rules for employee share schemes for many years. Business has responded favourably to these changes and I want to thank you for your success in simplifying this complex area.

I would like to give further consideration to two of your other recommendations for a 'marketable security' and an 'employee shareholding vehicle.' We will therefore issue a discussion document later this year to collect views from businesses, employees and share scheme experts on some of the important issues raised by these far-reaching proposals.



Competitiveness of UK tax administration

As you know, it is the Prime Minister's aim that the UK should rank in the top five countries in the world to do business within three years. The paper published by the OTS today sets out a credible programme of work, and I encourage businesses and groups with concerns about tax complexity to engage with this opportunity for reform. I look forward to reading your report later this year.

Finally, I would like to thank you and your team, for your work on these reviews. The OTS delivers remarkable value, bringing external challenge and perspective based on wide engagement with businesses and other taxpayers. I am confident that your recommendations will continue to deliver real simplifications that improve businesses and individuals' experience of the tax system.

Best wishes,

A handwritten signature in black ink, reading 'David Gauke'.

David Gauke MP

Government response to OTS partnership review

| | OTS recommendation | Government response |
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| 1 | HMRC to publish a manual of consolidated guidance for partnerships. | HMRC will publish a draft partnership tax manual for comment in April 2014. The manual will provide links to relevant partnership guidance in other HMRC manuals. |
| 2 | BIS to re-publish their model partnership agreement. | HMRC is working with BIS to publish a model partnership agreement and believes that this can be integrated within the consolidated guidance. |
| 3 | HMRC should add a box to the short return for partnerships to allow gross interest to be included rather than net. | HMRC to examine cost and feasibility of making the change. |
| 4 | HMRC should change the corporation tax self assessment return to include a section for income from a partnership. | HMRC already looking at the best way for companies to report partnership income. |
| 5 | HMRC to clarify when partnerships are eligible for entrepreneurs' relief. | HMRC will revise the guidance to clarify when entrepreneurs' relief is due. This will then be included in the HMRC partnership tax manual. |
| 6 | The process for issuing UTRs to foreign partners needs to be streamlined. | HMRC is already reviewing the process for some non-UK resident partners, and will look at the scope for further simplification. |
| 7 | It would be useful to have a form of general remittance basis investment relief for groups of non-domiciled individuals investing in UK investment partnerships. | HMRC will need to consider this proposal in more detail, however, it is very likely that the costs associated with |

Government response to OTS partnership review

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| | | the change will rule out taking this further. |
| 8 | HMRC to create free software for the smallest partnerships. | Production of free software for partnerships would involve significant costs and it is very likely that these will rule out taking this further. |
| 9 | HMRC guidance should be clearer on stamp duty land tax (SDLT) liabilities following changes in profit sharing ratio | HMRC will review the relevant guidance to make it clearer, and it will then be included in the HMRC partnership tax manual. |
| 10 | HMRC needs to review and update the guidance on inheritance tax for partnerships. | HMRC has worked with representative bodies to clarify this guidance (see Taxguide 01/14). This will be included in the HMRC partnership tax manual. |
| 11 | HMRC to clarify requirements as regards limited partnerships and joint ventures for the purposes of VAT registration. | This will be covered in revised guidance on VAT registration which will be published in 2014/15, and will then be included in the HMRC partnership tax manual. |
| 12 | HMRC to give clear guidance on VAT grouping for LLPs. | This will be covered in revised guidance on VAT registration which will be published in 2014/15, and will then be included in the HMRC partnership tax manual. |

Government response to OTS employee benefits and expenses review

| | OTS recommendation | Government response |
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| | HMRC administration | Chapters 1 to 5 |
| 1 | A legislative framework for employers to payroll some or all of their benefits and expenses on a voluntary basis (Chapter 1) | HMRC will consult on a proposal to introduce voluntary payrolling. |
| 2 | The scope of PAYE Settlement Agreements (PSA's) should be widened to permit employers to settle any tax liability on benefits and expenses (Chapter 2) | The Government believes that this proposal would not be consistent with the purpose of PSAs |
| 3 | Exemption for qualifying business expenses paid for or reimbursed by an employer (Chapter 3) | HMRC will consult on the design of an exemption. |
| 4 | £8,500 threshold to be abolished, but with simple mitigating steps and a consultation to confirm these (Chapter 4) | HMRC will consult on the effects of abolition and potential mitigation. |
| 5 | Defining in law a short, easy to understand 'principles based' definition of a trivial benefit, incorporating a per item cap, probably at £50 (Chapter 5) | HMRC will consult on the exact design of an exemption for trivial benefits. |
| 6 | Recommendations to reduce 'nil P11Ds', including a form to allow employers to indicate if a benefit is a one-off (Chapter 5) | HMRC will carry forward this recommendation. |
| 7 | Flat rate expenses (FREs) need to be reviewed and updated, and employers allowed to include employees' claims through the payroll (Chapter 5) | HMRC will consider ways of improving the administration of FREs. |
| 8 | HMRC's website should have a simple initial guide to employer's obligations with all relevant links (Chapter 5) | HMRC will carry forward this recommendation. |
| | Travel and subsistence | Chapter 6 |
| 9 | Legislation stating an employee can have only one permanent workplace, being the place | The Government will undertake a review of |

Government response to OTS employee benefits and expenses review

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| | <p>where they spend the greatest part of their working time. However, if costings show that this route would be too expensive for the Exchequer, we recommend amending Section 339 ITEPA 2003 to redefine “permanent” and “temporary” workplace by introducing a statutory percentage test, probably at 30 per cent</p> | <p>the principles and rules underlying the tax treatment of travel and subsistence expenses. The review will consider how the tax treatment of these expenses can be simplified best address the challenges of the changes to modern working and travel patterns.</p> |
| 10 | <p>A deduction for travel and subsistence expenses associated with a temporary workplace for the first 24 months regardless of the intended length of an assignment;</p> | |
| 11 | <p>A specific code for homeworkers with one clear definition of homeworking for all tax purposes</p> | |
| 12 | <p>Remove facility for employees to claim the cost of expenses not reimbursed by employers in working from home, provide an uplifted homeworking allowance, for example £10 per week</p> | |
| 13 | <p>A section added to ITEPA 2003 referring to ‘accommodation and subsistence expenses’</p> | |
| 14 | <p>In relation to benchmark scale rates, the guidance around ongoing checks should be amended to remove the requirement for employers to retain receipts</p> | |
| 15 | <p>Consideration is given to an exercise to modernise the rules for workplace lunches and canteens to improve consistency</p> | |
| 16 | <p>Where a deduction is available for attendance at a temporary workplace, living accommodation should be included in a P11D dispensation whether provided through hotel accommodation or use of a company flat (or equivalent)</p> | |
| 17 | <p>A formal, comprehensive study on the radical idea of all travel and subsistence expenses (possibly not including ordinary commuting), being allowable only if reimbursed by employer</p> | |

Government response to OTS employee benefits and expenses review

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| 18 | A formal review of tax reliefs for travel and subsistence should take place every ten years to make sure the system fully recognises changing work patterns | |
| | Longer term projects: structural changes | Chapters 7 and 8 |
| 19 | Alignment of the underlying definitions of income and expenses for income tax and NICs. This means aligning the bases on which income tax and NICs are calculated, such that the basis for charging NICs should replicate as far as possible that for income tax (Chapter 7) | In 2011 and 2012 the Government conducted detailed and extensive work with stakeholders regarding the operational integration of income tax and NICs. The outcome of this engagement was to wait until further progress with existing, planned changes to PAYE were made before proceeding further with this work. |
| 20 | The process should also look properly at the arguments for moving NICs onto an annual, cumulative basis (Chapter 7) | |
| 21 | Explore further the case for applying Class 1 NICs to all employee remuneration (whether cash or benefits in kind) (Chapter 7) | |
| 22 | The HMRC guidance provided for NICs and income tax should be reviewed and made consistent where possible (Chapter 7) | HMRC will carry forward this recommendation. |
| 23 | Fundamental review of the government policy on benefits. This should look at whether the government wants to tax cash or cash equivalents differently, whether the way a benefit is provided should determine how much tax is paid on it, and the question of what is a benefit and what is not (Chapter 8) | The Government will issue a call for evidence on remuneration and benefit provision in the 21 st century to inform future work. |