Tax and the Tax Authority's Responsibility

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In the July 2007 edition I wrote an article based on a conference I attended last summer entitled 'Tax and Corporate Responsibility'. I concluded that this would be followed up with two further enquiries, into the responsibilities of the taxing authority and of the individual taxpayer. This is the first, and it comes at an interesting time for me, as when this edition is published I shall be on secondment to the States of Jersey helping it implement Goods and Services Tax (GST), a form of VAT. I have used this as one case study as the questions it has posed and the responses of the tax authority highlight some of the key issues rather well. I have also drawn on my own experience of HM Revenue and Customs (HMRC).

A pre-consideration point here is that the tax authority, as a corporate body, is subject to the same obligations to corporate responsibility as any other such body. What was said in the first article holds good here too and I do not propose to re-visit, for example, obligations to suppliers, employees and neighbours. There is important common ground with commercial businesses, but there are also important differences, not least in the stakeholders and the authorities' relationship with them.

Until fairly recently HMRC's avowed commitment to corporate responsibility extended to the following 'internal' areas: equal opportunities, no discrimination of the basis of colour, creed, gender or sexual orientation, trying to limit waste of any form, and Investors in People (IIP). Regrettably it has been decided not to renew accreditation for IIP, partly on the grounds of cost. With the exception of IIP, all these areas are a matter of legal compliance, and while HMRC went beyond simple compliance in most respects the view of corporate responsibility was distinctly inward looking. Recently however this has been added to and elaborated by linking corporate responsibility more closely with corporate governance and in the past couple of years there has been an increasing emphasis on customer focus, putting "our customers first". At present HMRC is the only Whitehall Department to appear in the Sunday Times Top 100 Corporate Responsibility Index.

A recent re-ordering of the approach to corporate responsibility within HMRC has led to three critical areas being identified by the Corporate Responsibility Steering Group:

- the efficiency/staff relocation programmes;
- tax on the boardroom agenda; and
- marginalised customers.

An Action Plan is being developed and the Tax Credits Office chosen as the pilot area. In it there are seen to be four strands to Corporate Responsibility:

- understanding our customers and adapting to their needs
- protecting the environment for future generations
- managing the impact of our operations, products and services on society
- treating employees fairly.

The above helps identify groups of stakeholders, however an important distinction between a tax authority and a commercial organisation is that many key stakeholders are different, as are the priorities that arise from this. So who are the stakeholders? First and most important: the Government of the day. Jesus held up a coin and asked whose likeness it bore, the reply was "Caesar's". "Well then, pay to Caesar what is due to Caesar, and pay to God what is due to God." Implicit here is that it is government that sets the forms, scope and rates of taxation. The responsibility of the tax authority towards the Government is firstly then to implement and administer the tax in the prescribed way. There is here of course the debate of how the funds raised are spent, but this too is a matter for government and therefore outside the scope of this article. The tax authority is likely to have a great deal of influence over the design and interaction of taxes, but it is the Government that ordains what taxes are levied at what rates.

A good example of this is the decision to introduce GST in Jersey, which came about as a result of a decision to reduce company tax. Half of Jersey's Gross National Income is derived from financial services companies which have chosen to locate there to take advantage of the relatively low company taxation. In recent years other 'offshore' countries have sought to attract some of this business and to remain competitive Jersey has reduced company tax from 20% to zero and 10% (see http://www.gov.je/TaxMoney/ for fuller details). The resulting hole in the State's income has to be met from other measures, the chief of which is the introduction of GST from 1 May, 2008. GST will be simpler than VAT in the UK, with far fewer exceptions and exemptions, being imposed at 3% on the supply of most goods and services, including: education, medical services, food, and children's clothing. In practice it will be slightly regressive, those on lower incomes are likely to find the price increases a higher proportion of what they spend than the better off.

Two responses by the tax authority demonstrate how it has taken its corporate responsibility towards taxpayers seriously. Detailed modelling was carried out to estimate the effect of GST at different rates and on different household incomes. Using this data the authority recommended that a 3% rate coupled with an income support scheme for those on lowest incomes would both produce the required tax yield, net of the cost of income support and administration costs, and result in nil net income loss for those taxpayers. It is a good example of the duty of care being taken seriously and driving a workable solution. The second example is of charities, which are numerous, active and vital to Jersey life. As largely voluntary bodies they are unlikely to have the expertise or resources in house to administer GST, and the tax would normally fall as a cost on them, reducing their ability to undertake charitable work. A system of exemption is therefore to be introduced, whereby the Comptroller of Income Tax will, on application, issue a certificate to a bona fide charity so that suppliers do not have to charge it GST. The idea is that the certificates will only be issued for socially useful bodies (there is no legal definition of a 'charity' in Jersey), so the fun will start if, for example, sports clubs find their applications refused!

The second priority group of stakeholders are the tax collectors, and no – I don't mean me! It is a feature of modern taxation that taxes are predominantly collected by businesses and employers on behalf of the tax authority, and paid over on a periodic basis. Anyone who is whose tax and National Insurance is collected through Pay As You Earn (PAYE) will know this. Jersey GST is just such a tax, with the registered business able to offset the GST it pays out to it's suppliers against the tax it collects on what it supplies to others. There is an important principle arising from corporate responsibility here: proportionality. This manifests itself in two ways. Firstly the administrative burden on the business should be the least possible consistent with efficient administration of the tax. The costs of tax administration and compliance – PAYE, VAT, Corporation Tax returns for example – are a cost to the business and reduce profits. Yes, Corporation Tax is a (arguably over-complicated in the UK) tax only on profits, but businesses cannot set the *costs* of collecting, reporting and paying taxes such as employees income tax, Insurance Premium Tax or VAT against the taxes so collected. And the law of diminishing costs applies to businesses reporting these taxes: the cost of calculating, deducting and paying over Income Tax and National Insurance for its employees is not a hundred times greater for a company with 500 staff than it is for one man employing five others.

One of the things that has disappointed me (and there have been several!) in the brave new world of HMRC since it was formed in 2005 is how little colleagues working in one tax head understand of how other taxes impact on businesses. And it is not just across the two former departments either: in a recent programme of Cross Tax Awareness seminars I helped organise I was struck by how little debate there was about the impact on the example business of the various taxes involved. In the dozen or so events I sat in on only once did someone remark that the business would have to go into liquidation. At least there has been some progress from the scene that occasionally greeted me a few years ago, of arriving at a premises to find a couple of Excise officers already at work at the other end of factory and a team of Employer Compliance staff burrowing through the PAYE records. Businesses much prefer to deal through one point of contact and know that their tax affairs are being viewed in totality.

Then there is the burden of penalties and sanctions for getting it wrong. That there should be a regime of powers and penalties for errors and misdemeanours I think is uncontroversial. In recent years HMRC has viewed compliance with tax responsibilities as a spectrum, ranging from keen to get it right and put all the necessary systems in place to ensure it is, through accidental error or omission to carelessness, recklessness and eventually suppression with concealment. Those who cannot be encouraged and educated into compliant behaviours need to be penalised for two very good reasons:

it protects the integrity of the tax, and it supports equity of treatment. Why should the reckless or dishonest be able to compete against the careful and compliant? Here the tax authority has a great deal of influence, firstly in advising the Government on the powers and penalties regime then in ensuring it is used equitably and in proportion to the mischief done. Most taxpayers will never have heard of the Revenue Information Powers Act 2000, but it is an important piece of legislation, being a clear statement of how the principles set out in the Human Rights Act apply to how tax is collected. It is not – yet – an integral part of the training received by all HMRC tax officials, but will be soon.

Finally here there is the obligation of the tax authority to ensure that the information collected about taxpayers – individuals and corporate bodies – is only used for legitimate purposes and not divulged to a third party with has no right to it. Commercial confidentiality is only one aspect of this, unless there is a legally established and regulated gateway, information must not be exchanged between government departments. Although it concerned Child Benefit, not tax, the recent loss of data on 25m women and children in the UK by an arm of HMRC was a serious breach of this obligation and in my view the Chairman, Paul Gray, did 'the right thing' by resigning. It is all too easy to forget that the subject of the data in that file is a real person, to whom is owed an absolute duty of care.

There is one more primary group of stakeholders, those who work for the tax authority. Here its responsibilities are the same as any other large employer: for their health and safety, clear guidance and support on how to undertake their tasks, appropriate and timely training, consistent and reasonable management. Within any large organisation it is easy for an individual employee to lose sight of the overall purpose of the 'company', if they ever knew it in the first place. Thus training needs to be not only functional but also contextual, and not only one-off, 'box ticking', but continuous and supported. There has been some good progress here in HMRC, with a major re-structuring of technical training currently under way, clearly linked to career paths (both of which I've made significant contributions to – this is not time for false modesty!), and a top level commitment to Continuous Professional Development. If it is still falling short this is in my experience for two reasons: pressure on managers lower down the chain to deliver business results at the expense of training, and a lack of initiative on the part of staff themselves in seeking out opportunities.

One area affecting staff is having particular impact at present: technology. As so much more can be done on-line there is less of a need for local offices and paper files, thus staff numbers are being reduced – largely as far fewer processing posts are needed – and a programme of office closure and re-organisation is under way. From the organisation's point of view the moves are a reasonable response to changing business environment. For those affected they are made 'surplus' by their post and/or office disappearing, made to travel much longer to a new office – disrupting childcare arrangements for example. Here the tax authority has a responsibility to minimise or mitigate the impact of changes on its employees. Yet it is not, contrary to some views, in the business of job creation and some casualties are inevitable. And it is here that the MSE has a crucial role to play, not simply in the obvious pastoral role of binding the wounds but in pointing up opportunities for minimising and mitigating, in helping colleagues put together cogent cases for an action being taken in a different way or at another time, and raising a prophetic voice that points to a better way.

Perhaps more so than a commercial organisation, a tax authority is faced with maintaining a delicate balance between the often-competing demands of stakeholders. At least with the former most folk know that it is primarily in the business of making a profit for its shareholders by supplying X, Y or Z. A tax authority is too often seen as simply taking away the fruits of others' labour. First and foremost it is there to see that what is due to Caesar is paid to Caesar, as painlessly as possible. If Caesar's demands are unjust, that is not the fault of the collectors. Zachaeus, you will recall, was unjust not because he collected taxes but because he exceeded his authority. And in a democracy Caesar can be voted out.

In the final part of this trilogy rather more use will be made of biblical material in looking at the responsibility of the individual taxpayer. This is not to say that what we can glean (social security measure for the poor?) from scripture has nothing to say to the corporate, rather that the individual and the corporate are simply different sizes. But more of that next time……