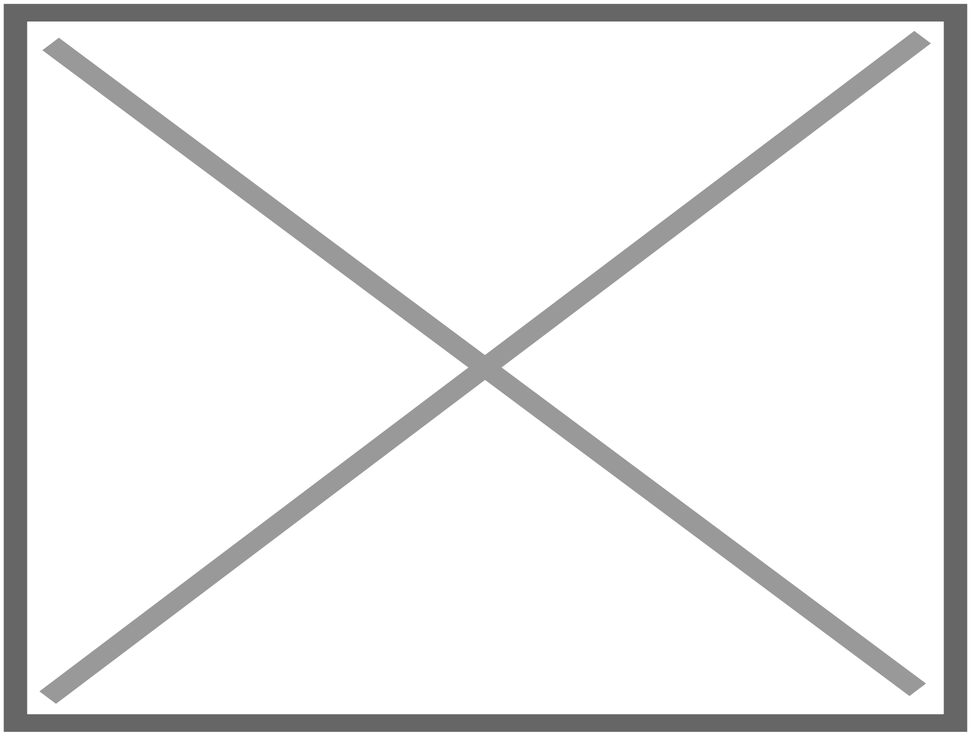
A new philosophy of tax

General Features   Management of taxes



06 September 2021

Bill Dodwell considers how better use of third party data could benefit individuals, their agents and HMRC, transforming the UK tax system

On 2 July, the Office of Tax Simplification published its report on ‘Making better use of third party data: a vision for the future’ (see bit.ly/3D2uCJ5).

What’s the report about? The intention behind it is to transform the individual tax system into one that uses 21st century technology. Put simply, the idea is that taxpayers would benefit if, instead of having to report some types of income and expense to HMRC, the relevant bank, pension company, investment manager or even charity could instead report the item(s). HMRC would then include the reported figures in the taxpayers’ online accounts with HMRC and, after checking, would use the information for tax codes and pre-population of self assessment tax returns. Tax agents would have access to the same information so they could use it to help prepare tax returns for their clients.

This report follows on from the October 2019 ‘Tax reporting and payment arrangements review’ (see bit.ly/2W68sEP), which looked at issues relating to self-employment income and rental income, where a third party or intermediary was involved.

Scope for change

The philosophy underlying both these reports is that we need to make better use of today's digital capabilities in our approach to tax reporting. The UK approach since 1944 has been that for the majority of taxpayers, a system of reporting and tax deductions would satisfy their tax obligations and ensure that they paid the right amount of tax. The PAYE system achieves a great deal for this majority, aided by the tax code which, when it operates perfectly, tailors tax deductions to the individual.

HMRC does receive some information on interest income and pension contributions currently, which is used where possible to help set tax codes. The problem, though, is that the information is received several months after the tax year and in a significant number of cases cannot be allocated to taxpayers.

Today, there is the scope to ask financial institutions (and potentially some other third parties) to take on additional or better reporting of customer data to HMRC.

The report discusses how banks and other financial institutions could report data to HMRC, which would then be visible to taxpayers in their forthcoming Single Customer Account. Taxpayers could check the data which would then be used in their tax codes and self-assessment tax returns – and ultimately for pre-population.

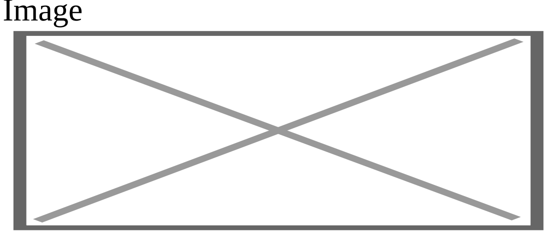
One of the most important discoveries in working on the report was that the majority of taxpayers, their agents and the financial institutions potentially involved gave a broad welcome to providing tax data to HMRC in this way. Naturally, taxpayers and providers both had a range of issues which would need to be dealt with should the government decide to take this work forward.

What is the Single Customer Account?

The Single Customer Account, available to view by taxpayers, will replace the current online Personal Tax Account and Business Tax Account, which have limited functionality. The new Single Customer Account will build on the current online accounts and add those digital services that are currently accessed separately through gov.uk, with the ambition to add further functionality.

The taxpayer-facing Single Customer Account will receive its data from HMRC's new Single Customer Record, which will sit behind the Single Customer Account to bring together the data held by HMRC on a taxpayer across the different taxes and data sources associated with a particular taxpayer. Third party data reported to HMRC would therefore be matched to a taxpayer's Single Customer Record, and then be visible to the taxpayer through their Single Customer Account.

Image



HMRC plans to give tax agents a view of the Single Customer Account data, probably through using third-party software with a link into HMRC's systems.

The Single Customer Account could – with suitable investment – become the hub for all interaction between the individual taxpayer and HMRC. The OTS's Claims and Elections report in October 2020 (see bit.ly/3mhseIw) highlighted that there are a wide range of claims and elections that could sit within an online account, potentially removing the need to submit a full tax return.

For many taxpayers, in time the Single Customer Account could remove the need to submit a self assessment tax return by allowing them to report income, claim expenses and check and verify information received by HMRC from financial institutions.

What data does HMRC currently receive?

HMRC receives some third-party data which is currently not always made directly available to taxpayers. It will be important to include this data in the Single Customer Account, as well as supplementing it with additional data. This includes:

- construction industry scheme data, which is likely to be available for taxpayers under HMRC's plans for Making Tax Digital for Income Tax;
- state pension data, which is available for some taxpayers, but not for all; and
- pension contribution data.

It will also include various employment information that is provided to HMRC by employers, who provide a copy to their employees, including:

- details of tax paid when an individual stops working for their employer (P45);
- tax paid on an individual's salary for a given tax year (P60) – generally included in the personal tax account at present;
- details of benefits in kind (P11D); and
- PAYE details of employee share schemes.

Additionally, HMRC receives annual information about bank and building society interest, as well as some other taxable interest (such as from NS&I). This comes some months after the tax year and cannot always be matched to taxpayer accounts. It is currently used where possible to issue tax codes but is not made visible to taxpayers except through the code.

What does the OTS report recommend?

The report recommends that the government and HMRC should extend the use and visibility of third party data to improve the accuracy of tax reporting and improve the taxpayer experience. This would include making the data held by HMRC from third parties visible to taxpayers and agents through the forthcoming Single Customer Account.

HMRC should use the data to update tax codes and make it available for individuals to use in their tax returns. Ultimately, this should enable the number of self assessment tax returns to be reduced, saving time and potentially cost for millions of taxpayers and for HMRC.

There are several important issues to be dealt with to take the project forward. The first point is that data exchange can only really be effective where taxpayers are assigned a unique identifier. Matching using our names and addresses is not sufficiently effective to achieve the very high level of accuracy needed for rapid data processing. The unique identifier most commonly used at present is the National Insurance number, which is held by almost all people over 16 and is already used for tax purposes. Currently, not every taxpayer has an NI number and so its use would involve extending the provision of NI numbers to all taxpayers. It would be possible to use a range of different identifiers, provided that they could be linked by HMRC. Other possibilities include the Unique Taxpayer Reference (currently held by Self Assessment taxpayers), a passport number (currently used with consent by HMRC for identification) or perhaps a driving licence.

Moving to much greater use of data provided by third parties to HMRC should involve a broadly based consultation about the balance of responsibilities between data providers, software providers, agents, taxpayers and HMRC, and the extent to which it is reasonable for taxpayers to rely on the data provided. The principle today is that taxpayers are responsible for the information in their returns. Should this change?

One important issue for taxpayers is the question of errors. Even with excellent systems and unique identifiers, properly verified, it is likely that there will be a small number of errors in information provided. It will be important for HMRC to set up an easy process for taxpayers to correct information – and provide more detail, in some cases. For example, some parents will hold accounts for their minor children. It may not be possible for the banks involved to identify this – and so designing a system to make it easy for taxpayers to pass on this detail to HMRC will be a vital part of building trust.

The big issue for potential data providers is having a clear roadmap for the stages in which greater use of third party data will be made, both to improve the way existing sources of data are provided and used, and to add further sources. Data providers will need templates to be set in advance to make it easier for their systems to pass the data appropriately to HMRC. Detailed consultation will be needed to get this right. HMRC will also need to invest in systems to receive high volumes of data securely and agree technology standards with industry bodies.

The report recommends that this work should progress in three stages – noting that the complexity of making some types of information available will mean that some information will be easier to provide earlier than other types.

Stage1:	Bank and building society interest Other interest Pension contributions Dividends and other investment income (initially voluntary)
Stage 2:	Excess reportable income (from overseas funds)
Stage 3:	Capital gains on sales of investments Chargeable event gains (insurance bonds

There would need to be a range of legislative changes to support the wider use of data provided by third parties. In some cases, it would be sensible to enable HMRC to process expense deductions without requiring formal claims. For example, at present an individual must claim higher rate tax relief for a pension contribution. However, where the information is received directly by HMRC, it should be processed without the need for that claim. There is some evidence that not everyone entitled to the relief knows how to make a claim to receive it. There would also need to be better ways for HMRC to receive the data without needing to make annual requests – and for third parties to submit data in the right format on a voluntary basis (which would require specific consent from their customers).

The adoption of the Single Customer Account and broadening the range of data provided automatically to HMRC should bring benefits to individuals, their agents and HMRC. This is a big change – but if done well, a worthwhile step forward to transform the UK tax system.