

Budget comment

View on policy

Overarching framework needed

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The Budget was, inevitably, far more about politics than taxation. Changes in tax were modest and thoroughly overshadowed by deficit closing, spending cuts, tax rises already announced (in the PBR) and tax rises yet to come (after the election). And, once again, those of us who look out for pronouncements on the overall direction of tax policy came away disappointed, though unsurprised.

This continues a pattern. Budgets and PBRs are usually rather short on big picture stuff. This is a shame: we surely need more attention paid to the way our tax system is developing, more thinking about how we are really going to get a tax system that will work for the 21st century and for business and general taxpayers (and for that matter advisers and authorities) that have to work with it.

There is an opportunity here – and a pressing need – for the next government to draw up an overarching framework for our tax system: to set out how it is going to be developed. We have a tentative step in this direction with HM Treasury's 'Tax Framework for Business', published formally with the Budget.

The final version shows little change from the draft and whilst it is hard to argue with the principles, the proof will be how it is applied in practice – especially as it gives the Government a get-out with adherence to the principles only 'where possible'.

This framework needs to be developed properly and with real commitments. Areas that spring to mind include:

- corporation tax: we need a system that will be internationally competitive; so let's be clear that the system is going to be developed with this in mind, that possible changes are going to be measured against the yardstick of 'will it help or damage competitiveness?';
- green taxes: as usual there were some tweaks in the Budget...but where are we really going with green taxes? How should businesses prepare?;
- consistency and commitment: can we have plans set out that will last (barring emergencies) for a good number of years? Can we have undertakings not to tinker and confuse?; and
- modernisation: there is a lot of good work going on in areas such as HMRC Powers; but can that zeal be applied to some of the backwaters (for example, out of date allowances) and with full appreciation of the impact in practice (so it suits taxpayers, not just HMRC).

And, above all, can Government really commit to proper development of legislation through consultation and a careful parliamentary process? Sadly, that is the last thing we are likely to get this time: we face the prospect a rushed, 2005-style Finance Bill as our representatives head off to campaign. It may not be a vote winner among the wider electorate, but the party that commits to doing tax policy and tax changes properly and on a long term basis might well gain – and would certainly deserve – some more votes from tax advisers.

Too much or too little?

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No-one can be surprised that the Budget failed to address the big economic questions, given the looming election. Few will have expected any radical tax changes. In view of the low expectations, does it make sense to call the Budget disappointing? Well, yes it does, because not only has the Budget done nothing very useful, but it has also created confusion about direction of travel in areas

where there was no need to do anything at all.

One example is the relationship between the financial accounts and taxable profits. Our tax system is increasingly reliant on accounting standards as a starting point for determining taxable profits, but the increased Annual Investment Allowance (AIA) moves in the opposite direction towards an expenditure base. Although this direction has its supporters and the increased allowance has been welcomed by small businesses and their advisers, how logical is it within the current tax system?

The AIA has some advantages over other small business reliefs, not least that it does not involve arbitrary thresholds in terms of the businesses to which it applies, but the problem is the perceived need to accompany the provision with complex anti-fragmentation rules, a disqualifying purpose rule (s 218A of the Capital Allowances Act) and now, it seems, yet another anti-avoidance rule to disallow property loss relief against general income to the extent that the loss is attributable to the AIA. A relief with a clearer economic rationale would have less need to be hedged about with purpose tests.

The need for these complexities arises because there is little logic in having an AIA that stops at £50,000 or £100,000.

The fact that this relief has simply been doubled at a stroke hints at figures plucked out of the air rather than having a clear basis. The emphasis on investment in assets as opposed to labour (in respect of which costs are increasing as a result of higher National Insurance Contributions) is also questionable given the nature of many small firms. It seems that those that do not require plant and machinery are seen as less in need of relief from tax than those that do. The rationale for this assumption is not clear.

A second example of lack of direction is the raising of the entrepreneurs' relief from £1 million to £2 million just two years after its introduction. This relief was never intellectually coherent and was a compromise from a government under pressure when it abolished taper relief. Increasing the limit does not make it any more rational. The predicted cost of this change is a relatively small £75 million in 2011–12, so this is an apparently large concession with limited real effect. Nevertheless it makes an illogical exemption that much harder to remove.

What is disappointing about this Budget is not that it does so little but that it was seen as being necessary to do anything at all in some of these areas.