

PO-CH/NL/0274

PART A

Part A.

SECRET

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Begins: 7/7/87.
Ends: 7/12/87.



PO -CH /NL/0274



PART A

Chancellor (Lawson) Papers:

INLAND REVENUE STAFFING
COSTS OF INDEPENDENT
TAXATION

By Independent Taxation

Disposal Directions: 25 Years

11/10/95.

PO -CH /NL/0274
PART A

TIMETABLE TO 1990
SUMMARY AGENDA

CONFIDENTIAL



THE BOARD ROOM
INLAND REVENUE
SOMERSET HOUSE

FROM: A J G ISAAC
7 JULY 1987

ISAAC
to
CH/EX
7/7

CHANCELLOR OF THE EXCHEQUER

INDEPENDENT TAXATION: TIMETABLE TO 1990: SUMMARY AGENDA

1. I have sent to you today a full note on the implications of adopting a 1990 start for independent taxation.
2. This summary note tries to pick out (without debate) some issues that you may wish to consider.

Legislation

- Perhaps a couple of dozen pages of legislation - perhaps with more (if you want to take up certain wider aspects, covenants etc) to follow in 1989?
- Aim to have decisions on main issue (independent taxation) before Recess plus early steer on likely other runners (transitionals, special cases, tax penalty on marriage) with remaining decisions progressed through summer and completed by October/early November? Some to be discussed with DHSS Ministers?

7 the PM?

cc	Chief Secretary	Mr Battishill	Mr Matheson
	Financial Secretary	Mr Isaac	Mr Crawley
	Paymaster General	Mr Painter	Mr Mace
	Economic Secretary	Mr Rogers	Mr Nield
	Sir P Middleton	Mr Pollard	Mr Glassberg
	Sir T Burns	Mr Lewis	Mr J C Jones
	Mr Cassell	Mr Beighton	Mr R H Allen
	Mr Scholar	Mr Cherry	Mr Yard
	Mr Cropper		Mr Marshall
			Miss Dyall
	Mr Jenkins (Parl. Counsel)		PS/IR

- Need for firm (therefore generous) decisions on peripheral issues, transitionals etc?
- Need for decision on priorities if other plans for the 1988 Budget would involve substantial additional development work at Telford?

Information technology resources

- Accepted that money will be made available as in present PES bid, to fund existing IT commitments?
- Additional provision for development work, hardware, software, running costs needed for independent taxation?
- Retain 10 to 15 middle management consultants in 1987/88, additional running costs of up to £1m (over and above current estimated deficit of £12.3m on running costs)?
- Defer desirable (but not significant staff saving) COP enhancements? Even so, acceptable some risk to timetable for and reliability of independent taxation, BROCS etc, or both?

The network

- Money available to fund PES provision for existing programme work in the network, necessary to give reasonable prospect that workstate is under control in 1989? Additional provision, to get work as up to date as possible?
- Additional staff costs for independent taxation of perhaps 1,200 or so from 1990/91, with setting-up costs rising from 100-150 man-years in 1988/90 to 650-750 in

1989/90, all subject to review when decisions taken and operational procedures worked out in detail?

Expenditure implications

- Very tentative estimates, subject to later review - and of course subject to your agreeing precise costings with us in due course - of costs of independent taxation, over and above existing PES bids, in region of perhaps:

	<u>Running costs</u>	<u>Capital</u>	<u>Total</u>
	£m	£m	£m
1988-89	4	2	6
1989-90	16	3	19
1990-91	24	-	24

- Additional running costs in 1987-88?

Subsequent changes in the timetable

- "Point of no return" - on the simple "go/no go" basis - not until April/May 1989? But inevitably costs and nugatory expenditure if decision to go ahead in 1990 taken now, reversed later?

Security

- Preparatory work to go ahead on a confidential and need to know basis - with explanation of "contingency preparations", if work becomes public knowledge?

AJG

A J G ISAAC



Inland Revenue

CONFIDENTIAL

Policy Division
Somerset House

FROM: B A MACE
DATE: 23 NOVEMBER 1987

FINANCIAL SECRETARY

*This and some
of the other
cases for a
share of
the total
with no
tax*

INDEPENDENT TAXATION: STAFF COSTINGS

MACE
TO
FST
23-11-87

1. This note reports the results of our recent work on the staff costs of Independent Taxation. As you know, privatisation has led to a substantial rise in the numbers of married women with dividends (but with little or no other income) who would be making repayment claims; and (as foreshadowed and already indicated to Treasury officials in the context of our PES discussions) this means an increase in our estimates of the cost of the new system. Mr Beighton's accompanying note therefore looks at options for ways in which these additional costs might be reduced by efficiency measures of one sort or another.

2. Following the outcome of the recent PES round, we have £m2.9 for Independent Taxation in our running costs provision for next year (1988/89); this includes the cost of 110 man-years of staff time. There is no provision at present for Independent Taxation in the following years; this will need to be taken into account in next year's Survey.

-
- Cancelled*
- | | | |
|------------------------------------|-------------|--------------|
| cc Chief Secretary | Chairman | Mr Davenport |
| Financial Secretary | Mr Isaac | Mr Nield |
| Paymaster General | Mr Painter | Mr Yard |
| Economic Secretary | Mr Beighton | Mr J C Jones |
| Sir P Middleton | Mr Matheson | Mr Eason |
| Mr Scholar | Mr Lewis | Mr Mace |
| Mr Culpin | Mr Cleave | Miss Dyall |
| Miss Sinclair | Mr Calder | Mr Boyce |
| Mr Cropper | Mr Crawley | PS/IR |
| Mr Tyrie | Mr Martin | |
| Mr Jenkins (Parliamentary Counsel) | | |

Staff numbers

3. As our earlier submissions have explained, the figure of 1200 or so which we have previously given Ministers for the additional staff numbers required for Independent Taxation was very much a "ball park" estimate based on a broad look at the extra work which would have to be undertaken by local tax offices to set up and subsequently run Independent Taxation. Over the last few months we have been looking in more detail at the new procedures which would be needed for Independent Taxation and attempting to quantify as precisely as we can at this stage the changes in workloads which will arise when married women become taxpayers in their own right. In particular, as mentioned in Mr Isaac's submission of 7 July, we have had to take account of new estimates of the number of married women who will be claiming payment of tax credits on dividends from privatisation and other shares. Although these new estimates of staff numbers are the best which can be made at this stage they are, for the reasons explained below, still subject to uncertainty.

4. The table below shows the latest estimate of the additional staff numbers required for Independent Taxation. The figures take account of the decisions which Ministers have so far taken on detailed aspects of the scheme (in particular on the treatment of the elderly and breadwinner wives). They do not, however, include the saving from the abolition of the minor personal allowances (100 units in a full year) which you and the Chancellor have provisionally decided should take effect from 1988-89. The figures for the additional cost of payments to married women of tax credits on privatisation and other shares are shown separately since they form a substantial part of the cost, and are particularly uncertain at this stage.

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Independent Taxation: Staff Numbers (man-years)

	<u>1988-89</u>	<u>1989-90</u>	<u>1990-91</u>	<u>1991-92</u>	<u>1992-93</u>
(a) Setting-up cost	150	770			
(b) Basic cost (excluding (c) below)			1250	1650	1400
(c) Cost of additional tax credit payments from privatisation etc issues			175-225	650-800	450-600
Total (man-years)	150	770	1425-1475	2300-2450	1850-2000

Note: the man-year need in the initial years does not all reflect permanent staff, but includes some casual staff and overtime. In addition the figures represent the units of work needed to run Independent Taxation by fully-trained staff. To achieve the appropriate manning levels in each tax office could mean additional transitional costs, for example because of staff inexperience. Whether this would be necessary cannot be determined until the appropriate PES round when we can take account of the manpower changes needed for Independent Taxation alongside other manpower changes which may be occurring at the time. But to the extent that it is necessary we shall need in PES to seek rather greater funding requirements for Independent Taxation than the figures quoted above suggest.

5. These latest figures show that the ongoing cost of Independent Taxation (excluding the cost of additional payments of tax credits) when the system has settled down in 1992-93 is not far off our previous "ball park" estimate. But the cost of

making payments to married women of tax credits on dividends adds around 450-600 to the 1992-93 total. This is because we estimate, on the basis of the information now available, that there could currently be between 800,000 and 1 million more married women seeking repayments compared with our previous forecast.

6. There is one important point we should make in relation to payments of tax credits to married women. The staff figures in the table above relate to the position as we think it is at present: in other words, they are based on the number of married women who are non-taxpayers and who at present hold assets (shares, unit trusts) on which we would be paying tax credits. But the announcement of Independent Taxation may cause people to change their behaviour in future in order to save tax. For example:

- (i) Wives may switch their existing investments, subject to the composite rate arrangements (eg bank and building society deposits) into investments paying interest gross (such as Post Office investment accounts* - implying a revenue cost but no new staff cost) and into investments where the income has tax deducted at source (such as equities, unit trusts and gilts - implying both an Exchequer cost and an additional staff cost).
- (ii) Married couples may transfer assets into their joint names, in order to gain tax relief on the wife's share of the income (implying both an Exchequer and a staff cost). This could take place in isolation (the equity share registered in the names of both husband and wife), or in combination with (i) above (the money now deposited with the bank in the husband's name, transferred to the Post Office Savings Bank in the joint names of husband and wife).
- (iii) Assets may be transferred outright from husband to wife, in order that the wife can claim tax relief on the income.

* At the upper end of the market, this could include bank deposits in the Isle of Man, Channel Island, Irish Republic etc.

7. Predicting the size of effects of this sort is very hazardous. But we are in a world where the mailshot, the financial institutions themselves and the financial pages of the daily press can exert considerable pressure. Behavioural effects might (we think) mean up to a further 1/2 million people claiming repayments, at an additional staff cost of (say) 300. We shall have to keep a careful eye on this and, as time goes on, assemble the best picture that we can.

Work in tax offices

8. It may be helpful if I explain briefly the work involved for tax offices in Independent Taxation and why the pattern of staff costs changes over the three year period 1990-91 to 1992-93.

9. First, Independent Taxation creates additional work in relation to the 5-6 million married women already on our books who will become taxpayers in their own right. Thus handling the tax affairs of married women directors and wives in husband and wife partnerships becomes much more staff intensive because tax returns have to be issued, more assessments have to be made and more statements of personal allowances given in partnership assessments have to be sent to partners. But there is a small consequential saving in that work on married men taxpayers should become easier. The costings take account of the shifts in work.

10. Second, Independent Taxation generates work on around 2 million married women not presently on our books, for example new Schedule D cases and new "Claims" cases where married women will be seeking repayments of tax deducted at source from investment income. The "basic cost" figures shown in the table in paragraph 4 include the staff costs of making repayments which we know will arise because details of income are already recorded in tax returns and reflected in the most recent Survey of Personal Incomes. The additional costs of making payments of tax credits on dividends on privatisation shares have had to be estimated separately from the available data about share-holdings

and are considerably more tentative. The new work is partly offset by a fall in the number of husbands presently liable to basic rate or higher rate tax and from other simplifications such as the removal of the need for the wife's earnings election (currently made by some 300,000 or so couples). These changes are also reflected in the costings.

Changes in Staff Requirement

11. Looking at the figures for staff numbers once Independent Taxation comes into force, costs are lower in 1990-91 than in subsequent years principally because a lot of the additional work for the first year of Independent Taxation does not arise until after the end of that year, when tax returns start to come in and assessments start to be made. Offsetting this, however, there are initial costs, mainly on repayment cases, which do not recur in later years. The figures for 1990-91 also include a larger element than in subsequent years, reflecting the additional staff costs which tax offices will have to bear in explaining the new system to taxpayers.

12. Staff numbers reach their peak in 1991-92, for three main reasons. First the additional work on tax repayments which will mainly arise for the first time in that year will have to be dealt with by tax offices mainly on a manual basis. From mid 1991 this work should be computerised and staff savings should therefore be achieved in 1992-93. Second there are some non-recurring initial costs in 1991-92. Third the figures for 1991-92 (like those for 1990-91) include an element for the work of explaining the change to the new system to taxpayers.

13. Subject to the uncertainties mentioned below the staff cost for 1992-93 represents our best estimate at this stage of the cost of running Independent Taxation once the new system has settled down (leaving aside the further impact of behavioural effects).

Uncertainties

14. As I have mentioned the figures remain subject to uncertainties at this stage and we shall be continually revising them over the next year or so as the Independent Taxation scheme is developed and tax office procedures are worked up in detail. Thereafter the figures will still be subject to further change as better data becomes available about changes in workloads once Independent Taxation starts running.

15. At present the main uncertainties are:

- (i) the extent of the likely behavioural effects (see paragraphs 6-7 above).
- (ii) The estimates for the staff cost of payments of tax credits on privatisation etc shares are particularly tentative and could be subject to substantial behavioural changes. The figures reflect the data currently available about holdings of privatisation etc shares from recent surveys and market research. But the picture is changing all the time and it is particularly difficult to predict how holdings of shares might have altered in two years' time when Independent Taxation is introduced. Recent events on the stock market and their effect on the previously expected take-up of BP shares by private individuals illustrate how uncertain any forecasts could be.
- (iii) The estimates assume the existing structure of income tax allowances and rates. If there were to be significant changes in the structure before Independent Taxation is introduced in 1990 this could affect the costings (either up or down).
- (iv) The staff costs shown in the table represent the net cost of Independent Taxation taking into account the costs of additional work on new married women taxpayers under the scheme and the savings as a result of the simplification

of the system. Both the components in this net figure are significant (the figure for 1992-93 for example includes a saving of some 700 staff as a result of the simplification of a husband's tax affairs under Independent Taxation and the removal of provisions such as the wife's earnings election and separate assessment). As a result, however, relatively small percentage changes either in the gross costs of the extra work or in the savings could lead to rather more significant alterations in the net cost of the scheme.

- (v) The costs are, of course, subject to future Ministerial decisions about the shape of the scheme (though we do not anticipate that any of the remaining points on which we shall be putting submissions to you in the next few weeks will have a significant effect on staff costs.)
- (vi) Finally we are currently updating the basis of our staff costings for repayment claims; this might mean some minor changes to the existing figures.

BA Mace

B A MACE

AJG 1/203/2

TASK FORCE SECRET

Copy No 2 of 25



Inland Revenue

The Board Room
Somerset House
London WC2R 1LB

*See
Analysis
(cf previous system).
X staff saws*

FROM: A J G ISAAC
23 November 1987

ISAAC
TO
FST
23.11.87

FINANCIAL SECRETARY

INDEPENDENT TAXATION - STAFF COSTINGS

1. These notes by Mr Mace and Mr Beighton report our estimates of the staff costs of independent taxation, and discuss some possible ways of minimising these costs.

2. As Mr Mace explains, our estimates of the basic costs of the scheme are reasonably well in line with the previous "ball-park" estimates. For reasons which we have already considered with you, however, the growth in the numbers of small shareholders since the estimates were first made, and in particular the success of privatisation issues, could add something in the region of 650 to 800 man years to the previous figures, plus the cost of possible behavioural changes which could add several hundred more.

3. I would emphasise four points, beginning with three major areas of uncertainty.

Chancellor

cc Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Mr Scholar
Mr Culpin
Miss Sinclair
Mr Cropper
Mr Tyrie

Chairman
Mr Isaac
Mr Painter
Mr Beighton
Mr Lewis
Mr Cleave
Mr Calder

Mr Yard
Mr Eason
Mr Mace
Miss Dyall
Mr Boyce
PS/IR

Mr Jenkins
(Parl Counsel)

4. First, there are the possible "behavioural" effects of independent taxation discussed in Mr Mace's note. There are potentially significant implications here, not only for staff costs, but also for Exchequer costs and competition within the financial sector. Following some initial consideration by the Treasury, we have assumed fairly modest changes of this kind. But there is a risk that "Money Which" and similar financial planning services could stimulate the wider spread of tax-efficient financial arrangements. However that may be, tax-induced developments of this kind could, of course, be swamped by developments (favourable or unfavourable) in the financial markets more generally.

5. Second, there are radical ideas now being discussed for taxing all investment income at a flat rate of (say) 35%, not refundable to individual taxpayers (the position of exempt funds is under consideration). If Ministers decide to pursue this option, we should have to take many of these plans back to the drawing board and (in the process) all these costings might wear a very different look.

X | 6. Third, we are separately reviewing some of the associated staff costs (eg maintenance and covenants).

7. Finally, the costings show something of a "hump", with staff requirements peaking in the introductory years. This is an inevitable feature of any major change, reflecting both the direct costs of setting up the new system and the need (which can take a lot of tax office time) to answer taxpayers' questions about the new system, to advise and guide them as they begin to learn how to work it, and to put matters right when they go off the rails. An additional factor in this instance is that we shall have to continue to handle repayment claims manually in the first year or so of independent taxation, before we can introduce computer support.

CLOJ

CONFIDENTIAL



FROM: FINANCIAL SECRETARY
DATE: 7 December 1987

FST
TO
CH.
7-12-87

CHANCELLOR

cc Chief Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Cassell
Mr Scholar
Mr Culpin
Mr Cropper
Mr Tyrie
Mr Battishill - IR
Mr Isaac - IR
Mr Beighton - IR
Mr Mace - IR
PS/IR

INDEPENDENT TAXATION

I have discussed with officials Mr Culpin's minute of 4 December, Mr Mace's minute of 4 December and Mr Beighton's minute (dealing with the cost of handling claims) of 23 November.

2. I think that Mr Culpin's minute represents a useful attempt to stand back, examine where we have got to and to consider how it all looks. I believe our decisions stand up pretty well to this treatment.

3. However, my discussion did throw up a couple of issues which will feature prominently in the presentation:

- i) Is independent taxation just a half-way house on the road to transferable allowances (or Mandatory Separate Taxation)?
- ii) Why keep a married couple's allowance?

Half-Way House?

4. I believe that we should say that transferable allowances are not on for the foreseeable future (no consensus reached etc) and then defend independent taxation on its own merits. It provides independence (ie privacy and disaggregation); it recognises marriage (would advocates of Mandatory Separate Taxation have us taxing capital transfers between spouses?); and it compares favourably on cost and simplicity against other conceivable options. There should be no suggestion that this is just a first step (and is therefore by implication inherently unsatisfactory).

Married Couple's Allowance?

properly
5. This has to be defended on distributional grounds. If it were abolished then the tax threshold for millions of taxpayers would fall, with large numbers forced into the poverty trap. Abolition would fly in the face of our Green Paper objective of helping one-earner couples. It was also a highly controversial pre-election Labour Party proposal - we can claim a mandate for its retention.

Details

6. Two points struck me on Mr Mace's minute of 4 December

i) BES relief;

ii) The structure of the Married Couple's Allowance.

BES

7. It does seem to me to be very generous to give both husband and wife a £40,000 limit. However, I suppose this is consistent with what is proposed on other joint limits (except perhaps mortgage interest relief and life assurance premium relief). I am considering further the BES starter.

Married Couple's Allowances

8. It is a great pity, in my view, that we could not introduce a "proper" couple's allowance, fully transferable between spouses

Instead of this cosmetic change. It is too late now to change this for legislation in 1988. We will have to consider how best to present it.

Staff Costs

9. I have also considered Mr Beighton's minute of 23 November which looks at the impact of wider share ownership, combined with independent taxation, on staff requirements in the Revenue.

10. The present estimated on-going staff cost of independent taxation is approaching 2000 (of which up to 600 results from additional tax credit payments from privatisation issues and so on). This compares with an initial (highly tentative) estimate of 1200 or more (Mr Mace of 7 July). The Revenue obviously have no PES provision for years post 1988/89 - the on-going costs of 2000 or so do not in any case come through until 1992/93.

11. Against this background I have considered whether any of the proposals in Mr Beighton's minute would be worth taking further. Of course, were a withholding tax to be introduced we would have to think again.

Centralising Claims Work

12. I think this should be looked at, although at first blush it does not seem promising, since there is virtue in having local access and also, more importantly, claims work tends to be rather seasonal.

Restriction of Insufficient Claims

13. I think this too is worth looking at. There would be an adverse cash-flow effect on people making small claims throughout the year, who would not get repayments until the limit were exceeded. But they would eventually get the money owed. I have asked the Revenue to examine three possible limits: £50; £100 and £200 and also to examine whether, if the restriction applied to charities making claims, many would in practice be affected.

Restriction on Size of Claim

14. I find this thoroughly unattractive. In order to be in receipt of a dividend of £30 or more from any of the recent

privatisation stocks, an investor would have had to put in substantially more than the minimum investment level. I do not see how we could defend this at all.

9.11.

ff- NORMAN LAMONT