Funding the Future

HMRC are going to impose costs of Â£1.8 billion on th...

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I issued this press release last night:

Making Tax Digital

HMRC gets its estimates seriously wrong and small business will pay £1.8 billion as a result

Evidence in support of the statements made to the

House of Lords Economic Affairs Committee by

Richard Murphy FCA

Professor of Practice in International Political Economy, City, University of London

A [new report] **by tax campaigner and academic Professor Richard Murphy casts doubt on HM Revenue & Customs' claim that its Making Tax Digital programme will save the UK's businesses £100 million a year. He does instead suggest that it will cost those businesses at least £1.8 billion a year, or an average of £305 for each of the 5.9 million businesses HMRC says will be affected by Making Tax Digital. £1.8 billion is fifty per cent of the annual running costs of HMRC in 2015/16.**

Forensically analysing the numbers in a report prepared to support evidence he will present to the House of Lords Economic Affairs Committee on 6 February Richard Murphy found that HMRC expects it will cost the average small business no more than £4.36 to prepare, summarise and submit their accounts for each three month period. Richard Murphy said:

"HMRC assume that the maximum additional cost small business will pay to comply with the Making Tax Digital Programme will be £170 million, including software costs. Stripping out the smallest estimate I could make of those

software costs left just £103 million to cover the cost of 5.9 million businesses submitting four extra sets of accounting data a year, each of which will have to be right if penalties are avoided. Simple division suggests each will cost £4.36 in HMRC's view in that case."

Richard Murphy added:

"HMRC's estimate suggests they think a person paid the UK minimum wage should be able to prepare and submit quarterly accounts for a UK small business in just 35 minutes. That is, of course, impossible. In my evidence to the Lords I have suggested the tasks involved. I estimate an average one-person business might take half a day to do this. Based on annual average self-employed earnings that represents a cost of £108 a year. However about two thirds of all small businesses and 78% of companies seek help with their tax returns. If they do that with Making Tax Digital returns, as seems likely, I think their costs will vary from £300 to £600 a year. Only small landlords might get away with additional costs of no more than £100 a year. That's how I come to an estimate of £1.8 billion including software costs'"

Concerning HMRC's claim that taxpayers will actually be better off as a result of Making Tax Digital returns Richard Murphy said:

"After getting their cost estimates for Making Tax Digital wrong HMRC then make the quite surprising claim that small businesses will in fact on average be £17 a year better off as a result of complying with the process because of the value of the information the new system will supply them with. I disagree. As an experienced chartered accountant I know that most small businesses have little idea what accounting data means. They do instead use simple rule of thumb measures to indicate how well their businesses are doing, and in most cases these are all they need. There's no substance to HMRC's claim for any benefits arising to these businesses."

He added that HMRC's claims that additional tax will be due are also wrong:

"HMRC's claim that more than a billion pounds of extra tax will be collected as a result of Making Tax Digital includes some pretty basic errors and some questionable assumptions. They start by assuming all errors in tax returns are now made by small businesses, but that is not true. Their own data shows that only half the tax gap is the fault of SMEs. That means their estimate of tax to be recovered is double any likely amount of tax collectable. What is more, they also assume that doing accounts four extra times a year against very tight deadlines will reduce the error rate. There's a much greater chance that time pressure alone, coupled with resentment and an inclination to make estimates to get returns in on time to avoid penalties will in fact considerably increase the error rate in small business accounts and so the UK tax gap."

Professor Murphy, whose own estimate of the UK tax gap is almost three times higher than that of HMRC noted that:

"New evidence from the National Audit Office that I noted for the first time when preparing the report suggests that the UK tax gap in the small business sector may considerably exceed HMRC's own estimate of total losses to this sector. Only a tiny part of that gap might really come from accounting errors. Instead of imposing substantial new burdens on the those in the UK small business community who are already trying to be tax compliant HMRC should instead be chasing those who duck out of the system altogether. That's where the real problem lies and the number doing so is bound to increase as many small businesses move into the shadow economy rather than face these massive new admin burdens from HMRC."

Richard Murphy expressed additional concerns:

"Not only are HMRC imposing new accounting burdens on small businesses they're also suggesting those businesses abandon proper accounting methods and use cash flow accounting in their place. Cash flow accounting is dangerous. It makes your business look good (and will give you a bigger tax liability in the future) if you simply stop paying your suppliers. But this is deeply misleading. It's hard to estimate how many business's HMRC might send to the wall by encouraging reliance on this deeply misleading method of accounting, but some will go that way as a result. No tax system should encourage such an outcome."

Talking of failure to disclose information when required, Professor Murphy said:

"It is rather surprising that HMRC has never said what it think Making Tax Digital will cost it. What we do know however is that it intends to get rid of 5,000 staff working in this area by 2020. Taxpayers are shouldering an enormous burden so that HMRC can claim it is more efficient. This makes no sense for the UK economy as a whole."

Putting his academic hat on for a moment Professor Murphy said:

“It is appropriate to note that Adam Smith identified four maxims with regard to the management of taxation in 1776 in The Wealth of Nations. These were that tax should be equitable, certain, convenient and efficient. There is no evidence at all that MTD is equitable, convenient or efficient. The only thing certain about it is that it will impose considerable additional cost on taxpayers. It is very unlikely to close any tax gap. It is hard to think of a policy more antithetical to the culture of enterprise in the UK than MTD as HMRC propose to impose it.”

Ends

Notes to editors:

Richard Murphy is presenting evidence to the House of Lords Economic Affairs Committee at 3.35pm on 6 February 2017. The full report on which this press release is based is available at ***http://www.taxresearch.org.uk/Documents/MakingTaxDigitalFull.pdf . Full references to all data referred to are available in that report.***

Professor Richard Murphy is Professor of Practice in International Political Economy, City, University of London. He is also director of Tax Research UK and blogs at http://www.taxresearch.org.uk/Blog/ . A summary CV is available in the full report.

Richard Murphy's new book 'Dirty Secrets: how tax havens destroy the economy' is published by Verso on 7 February.

Richard Murphy's work on the tax gap and related issues is undertaken as part of Coffers (Combating Financial Fraud and Empowering Regulators), which is an EU funded Horizon 2020 project. Full details are available in the main report.