TAX JOURNAL

Views from business on the coalition's tax policies and priorities for a new government

Report of a Tax Journal/Pinsent Masons Survey May 2015

Executive summary

75 in-house tax directors and heads of tax from large companies took part in a recent survey on the coalition government's tax policies and priorities for the new government.

Key findings are:

- **Tax competitiveness:** There is overwhelming agreement (92% of respondents) that the coalition has been successful in delivering 'the most competitive corporate tax regime in the G20, while protecting manufacturing industries'.
- **Interest deductions:** 96% say the current tax treatment of interest deduction is very important or important to UK tax competitiveness.
- **Diverted profits tax:** 71% say that the UK's new diverted profits tax, introduced last month, has undermined UK competitiveness.
- **Infrastructure:** 61% say the tax system does not adequately support infrastructure investment.
- **Enforcement and compliance:** 73% say the process for resolving disputes is about the same as it was in 2010; 64% say HMRC's litigation and settlement strategy works well 'on the whole'; and 55% think accelerated payment notices are a good idea.
- **Base erosion and profit shifting:** A little over half of respondents believe the OECD's project on BEPS will not deliver its stated aims.
- **Priorities for a new government:** Protecting the current tax treatment of interest deductions emerged as the top priority for the new government, marginally ahead of maintaining the 20% corporate tax rate or cutting employment taxes.

Analysis

Seventy five in-house tax directors and heads of tax from large companies, including those in the FTSE 100, took part in a survey by *Tax Journal* and law firm Pinsent Masons to give their view on the coalition's tax policies and identify priorities for the next government.

A competitive tax regime

When the coalition government took office in May 2010, it said in its agreement that: 'Our aim is to create the most competitive corporate tax regime in the G20, while protecting manufacturing industries.' Around 92% of those polled (69 out of 75) rated the coalition government as having been 'successful' (80%) or 'very successful' (12%) overall (see figure 1 below).

One commented that 'policy has become more unpredictable and, in recent years, more political'. Another added that: 'They have been trying to do the right big-picture things, in the main. But they still haven't got to grips with the need for simplicity and certainty, and have given in to the media-led demand for "something to be done" about perceived tax avoidance.'

About 63% said that the lower headline rate of corporation tax, as set out in the *Corporation Tax Roadmap* (2010), boosted investment or growth in their own company in the UK; however, the vast majority of those respondents admitted this was to a marginal degree rather than a greater one.

Also 59% rated the patent box as having been successful or very successful.

More significantly, 96% of those surveyed said they felt the current treatment of interest deduction was either very important or somewhat important to UK tax competitiveness (see figure 5 below). 'Putting the five-year roadmap in place which confirmed interest deductibility would be protected, as well as the direction of travel on corporate tax rates, etc was an excellent idea, as it gave a high level of certainty on the UK corporate tax regime for this parliament,' one respondent wrote.

'The *Corporation Tax Roadmap* was a good idea and it has generally been adhered to,' another said. 'A consistent approach has avoided nasty surprises and encouraged investment. The consultation on proposed budget changes in 2010 and the rethink on slashing capital allowances was particularly welcome and demonstrated that the coalition was prepared to listen. I think the presence of David Gauke at HM Treasury throughout the term of the government has been an important factor in ensuring consistency of approach.'

However, 61% of participants said the tax system does not adequately support infrastructure investment, with a number of respondents commenting about complexity, uncertainty and the lack of the long-term vision which is so crucial for projects which typically have a long lifespan.

Policy making

There were mixed views on whether the coalition's new approach to tax policy making met its stated aims of '[restoring] the UK tax system's reputation for predictability, stability and simplicity' (as set out in the 2010 HMRC/HM Treasury document *The new approach to tax policy making*).

57% of the surveyed heads of tax and tax directors felt the new approach was successful or very successful, although one observed: 'Over the lifetime of the coalition, there have been tax "raids" on the oil companies and the banks; and, more recently, the diverted profits tax was pulled from the hat like a bewildered bunny. Some belated relief has been given to the oil sector this year, but these three areas show that "predictability, stability and simplicity" do not always get a proper hearing.'

'I applaud the consistency that the coalition has shown on building on the previous government's policies,' another commenter said. 'However, a lack of certainty remains – few opportunities for rulings, constantly changing legislation driven by interfering politicians, and unexpected legislation introduced too quickly with minimal consultation, e.g. for the diverted profits tax (DPT). There's an increased compliance burden with the diverted profits tax and the new BEPS driven transfer pricing. The CFC financing exemption is important for UK competitiveness today, but it is likely to disappear when the EU challenges it, so competitiveness could decline significantly.' Another added that the plan set out by the roadmap had been 'largely good except for the bank levy – increases in rate to meet a fixed target make it difficult to price fairly to customers, and the levy is ultimately borne by customers of banks.'

Figure 1: The big picture

When the coalition government took office, it said: 'Our aim is to create the most competitive corporate tax regime in the G20, while protecting manufacturing industries.' (*The coalition agreement*, May 2010).
How would you rate the coalition's success overall?

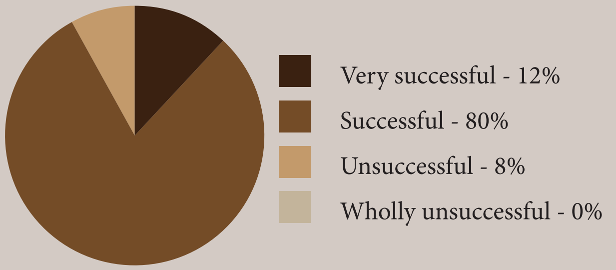
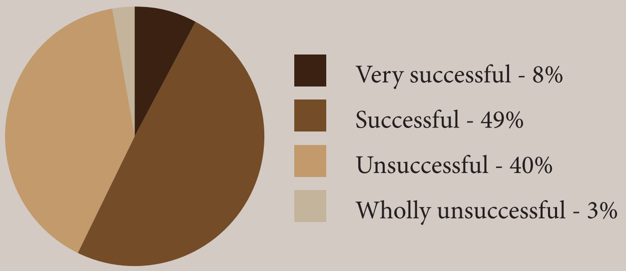


Figure 2: The new approach to tax policy making

The coalition government implemented a new approach to the way in which tax policy was made 'to restore the UK tax system's reputation for predictability, stability and simplicity'. (*The new approach to tax policy making*, 2010).
How would you rate the success of this new approach?



The diverted profits tax and BEPS

Much was said about the controversial DPT, which came into force on 1 April (see figure 6 below). A significant number of respondents (71%) said the DPT has undermined UK tax competitiveness, with a number expressing concern that the UK's unilateral action in introducing the tax could lead to double taxation, unpredictability and complexity if others follow suit. The remaining 29% either believed the DPT didn't undermine the UK's tax competitiveness significantly (21%), or that it was necessary 'to ensure companies pay a fair amount' (8%).

'The UK seems to lag behind in using tax policy to its full potential, for instance, in encouraging environmentally sustainable investment decisions,' began one comment. 'The current allowances regime is too narrow. The UK should also resist the urge to act politically, with the DPT being the key case in point. There are already sufficient safeguards in place (arm's length transfer pricing, CFC, withholding tax); just change the thresholds/rates if they aren't working (but they are). The DPT introduces uncertainty and signals a worrying shift in policy to a subjective analysis of what is the correct amount of profits to tax (arm's length, etc) to a new unclear basis.'

'The coalition government deserves a lot of credit for the approach it took to corporation tax,' said another. 'However, I think it has made mistakes in way the DPT was introduced and in playing politics with tax on BEPS. The government seems to want to play the political card at the risk of undermining the UK competitive tax regime.'

Commenting on the survey, Pinsent Masons partner Heather Self added: 'We said at the time that DPT was poor legislation, introduced in too much of a rush. We hope that the new government will think again on this subject.'

Despite the criticisms of the DPT, a little over half (55%) of respondents were sceptical that the OECD's BEPS project would meet its objectives (see figure 8 below). The opinions expressed were wide ranging: one responded it would be 'a marginal "yes" … but there will be uncertainties and mismatches in the final outcome'; while another described it as 'surprisingly good progress and the process seems to have welcomed engagement with business and been open to suggestions. The UK's decision to go ahead with DPT is difficult to understand given the recognised need for coordinated action and success will only be achieved if all jurisdictions commit to the process.'

Meanwhile, others said it was 'a sledgehammer to crack a nut', 'misguided and misdirected', while another observed: 'It's trying to do the right sort of thing, but like many other EU-led initiatives it will become mired in bureaucracy and a legalistic approach and it will be hard to get a consensus which can be implemented practically within finite time.'

Other views noted the challenges inherent in getting all countries to comply (especially the US) or co-ordinate implementation efforts, and the risk of double taxation on profits.

Enforcement and compliance

On enforcement and compliance, 73% of respondents said the process for resolving disputes has neither got better or worse during the coalition's term in office, with 24% believing it had got worse. Almost two thirds (64%) said HMRC's litigation and settlement strategy (LSS) works well in practice 'on the whole'; and there were mixed views on whether accelerated payment notices are a good idea – with 55% saying they are.

James Bullock, head of litigation and compliance at Pinsent Masons, noted: 'At first blush HMRC might take heart from the fact that 64% of respondents expressed the view that the LSS "worked well, on the whole". However, we note that a very significant minority – some 32% of respondents – expressed the view that LSS did "not really" work well. That figure is astonishingly high … The whole question of tax dispute resolution – and the LSS in particular – has to be one of the issues that is looked at very closely by the next government. There are simply too many tax disputes that remain unresolved.'

Priorities for the next government

The top concern for in-house tax directors and heads of tax was

Figure 3: Corporation tax rates

'The government believes that the headline rate of corporation tax is important to the UK's competitiveness. Reducing corporation tax rates benefits businesses across the economy and can boost investment and growth' (*Corporate Tax Roadmap*, 2010).
Has the reduction in corporation tax rates boosted investment / growth of your company in the UK?

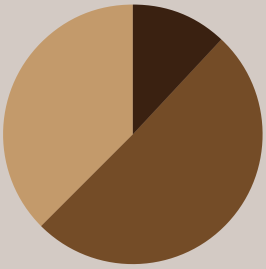
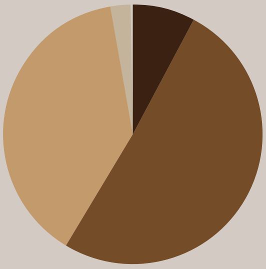


Figure 4: Patent box

The Patent Box was introduced with the aim of encouraging 'companies to locate the high-value jobs and activity associated with the development, manufacture and exploitation of patents in the UK. It will also enhance the competitiveness of the UK tax system for high-tech companies that obtain profits from patents.' (*Corporate Tax Roadmap*, 2010).
How would you rate its success?



for any future government to protect the current tax treatment of interest deductibility (see figure 12 below). Pinsent Masons partner Eloise Walker said any restrictions on interest deductibility could have a 'particularly detrimental effect' for infrastructure projects which tend to be very highly geared, and many of which already suffer tax at much higher rates than the standard 20% 'thanks to the current lack of any proper infrastructure allowances for such capital assets in the UK'.

Other priorities which respondents felt were important were a commitment to maintaining the corporation tax main rate at 20%, and cutting employment taxes.

Many other suggestions for future tax policy were made, including:

- the continuation of publishing draft legislation for consultation;
- retaining and expanding the OTS;
- properly resourcing HMRC, training its staff and restoring public confidence in the organisation;
- allowing the OECD to complete its work on BEPS without taking any further unilateral action;
- the reform of business rates; focusing on reducing tax complexity, rather than anti-avoidance; and
- reissuing a further five-year corporation tax roadmap.

'Focus on simplification of the code, rather than anti-avoidance – and be bold,' urged one respondent.

'Take the politics out of it,' suggested one. 'Aim for simplicity. Send Margaret Hodge on a course entitled: "If you don't agree with the current legislation, change it" – this is your job and stop throwing stones at corporates for political ends.'

Several respondents commented on HMRC's role. 'Do not forget that HMRC has to operate the policies and needs support. Business has high regard for HMRC and it is a critical part of a competitive UK, it would be very damaging to lose this,' said one respondent.

'HMRC needs to be properly resourced, trained and motivated, and needs to be supported at all times by senior management and politicians,' said another. 'The work of the Board's Solicitor needs to be reviewed, as the present impression is that those people are useless.'

However, 'HMRC now has too much power,' observed a third. 'Only those persons with deep pockets and access to good advice have any hope of getting justice if HMRC turns against you. The law is too complex and in too many places it is dependent on the right "intention" to get the right result. This makes effects very subjective and very difficult to plan around. Uncertainty is the greatest hindrance to investment.' ■

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Verbatim comments

Reproduced below are verbatim comments from respondents on the coalition government's tax policies; BEPS; and priorities for a new government.

Views on coalition's tax policies

- The key factors are diverted profits tax and hybrids. I'm writing this on a visit to the US where we are discussing restructuring proposals. The favoured location is now seen as Luxembourg, precisely because DPT and the attack on hybrid finance structures tell them that the UK is not serious about being open for business.
- Policy has become more unpredictable & in recent years more political.
- Limited relief for 'industrial' buildings – admittedly removed by previous government – does lead to much expenditure obtaining no relief.
- They have been trying to do the right big-picture things, in the main. But they still haven't got to grips with the need for simplicity and certainty, and have given in to the media-led demand for 'something to be done' about perceived tax avoidance.
- Coalition government deserves a lot of credit for approach it took to corporation tax. I think it has made mistakes in way DPT was introduced and playing politics with tax on BEPS. Seems to want to play the political card at the risk of undermining UK competitive tax regime.
- Over the lifetime of the Coalition there have been tax 'raids' on the oil companies and the banks, and more recently the Diverted Profits Tax was pulled from the hat like a bewildered bunny. Some belated relief has been given to the oil sector this year, but these 3 areas show that 'predictability, stability and simplicity' do not always get a proper hearing.
- The *Corporation Tax Roadmap* was a good idea and it has generally been adhered to. A consistent approach has avoided nasty surprises and encouraged investment. The consultation on proposed budget changes in 2010 and the re-think on slashing capital allowances was particularly welcome and demonstrated that the coalition was prepared to listen. I think the presence of David Gauke at HMT throughout the term of the government has been an important factor in ensuring consistency of approach. Whenever I have heard him speak about tax it's been worth listening to (all politics aside).
- Largely good except for the Bank Levy – increases in rate to meet a fixed target make it difficult to price fairly to customers. Ultimately borne by customers of banks.
- Introduction of anti-avoidance legislation at speed and without consultation at a time when BEPS was moving along at pace has blemished a good record.

- Depends what industry you work in.
- Any UK government must consider the UK's need for infrastructure across a 20 to 30 year time horizon. The Coalition government's tax policy does not suggest they are thinking that far ahead.
- There is still a marked degree of complexity and uncertainty within the tax system that would deter private investment in national infrastructure.
- I applaud the consistency that have shown on building on the previous governments policies. However, lack of certainty remains – few opportunities for rulings, constantly changing legislation driven by interfering politicians, unexpected legislation introduced too quickly with minimal consultation (diverted profits tax). Increased compliance burden with diverted profits tax and new BEPS driven transfer pricing. CFC financing exemption is important for UK competitiveness today but is likely to disappear when EU challenge it, so competitiveness could decline significantly.
- There were some good, well consulted and economically sound tax policies, but often spoilt by a couple of politically/media-driven, under-consulted tax policies. As with all recent governments, the tax system at the end of the government is much more complex and unwieldy than it was at the start. Finally, consultation on improving parts of the tax system often stymied by having to be fiscally neutral – if a poor tax needs to be reformed to a better but lower yielding tax then the tax-take from that tax should be allowed to fall.
- Broadly positive in the early years but regressed quite significantly towards the end due to being unduly influenced by populist sentiment, which was quite often ill informed.
- The UK seems to lag behind in using tax policy to its full potential, for instance, in encouraging environmentally sustainable investment decisions. The current allowances regime is too narrow. The UK should also resist the urge to act politically. Diverted profits tax being the key case in point, there are already sufficient safeguards in place (arms length TP, CFC, WHT), change the thresholds/rates if they aren't working (but they are). The DPT introduces uncertainty and signals a worrying shift in policy to a subjective analysis of what is the correct amount of profits to tax (arm's length etc) to a new unclear basis.
- Putting the five year corporate tax roadmap in place which confirmed interest deductibility would be protected; which confirmed the direction of travel on corporate tax rates etc was an excellent idea as it gave a high level of certainty on the UK corporate tax regime for this parliament.
- Business rates requires fundemental reform and is a significant inhibitor to certain business sectors.

Views on BEPS

- Expect that it, in reality, it will be very difficult to get alignment between countries on many of the issues and so project won't actually deliver on many of its Actions.
- I agree it has the potential to do this. However, even the developing language in this area (BEPS resilient versus BEPS compliant) implies that it will be harder and take longer than the OECD anticipates. I believe it is therefore a mistake for the UK to pre-empt BEPS outcomes.
- If anything it seems to add a great deal of extra compliance and uncertainty into the process on straightforward transactions and seems designed to introduce a restriction on deductions on perfectly normal business activities. It is a sledgehammer to crack a nut.
- [It should deliver] with the caveat 'eventually'
- BEPS will be a menu of options which jurisdictions picking the options they like and to a certain extent using it as an excuse for draconian measures.
- Challenging to pull overlapping workstreams into a coherent whole. US commitment to impementation uncertain
- It is likely to take a long time for co-ordination of all countries' policies to have much impact
- Trying to do the right sort of thing. But like many other EU-led initiatives it will become mired in bureaucracy and a legalistic approach and it will be hard to get a consensus which can be implemented practically within finite time.
- Jury is out on BEPS. Will only be able to judge impact when countries start to legislate. But early signs are not encouraging as looks as if it will lead to significant double taxation
- In theory BEPS should produce better coherence and bring effects and benefits in line with international expectations. I fear that in practice the likely paralysis in US law-making, the expected land grab of taxing rights by the BRICs and the unhelpful political effect of the DPT will only decrease certainty and predictability.
- Surprisingly good progress and process seems to have welcolmed engagement with business and been open to suggestions. UK decision to go ahead with DPT is dificult to understand given the recognised need for coordinated action and success will only be achieved if all jurisdictions commit to the process.
- The BEPS action plan is misguided and misdirected.

Figure 5: Interest deductions

How important is the current treatment of interest deduction to UK tax competitiveness?

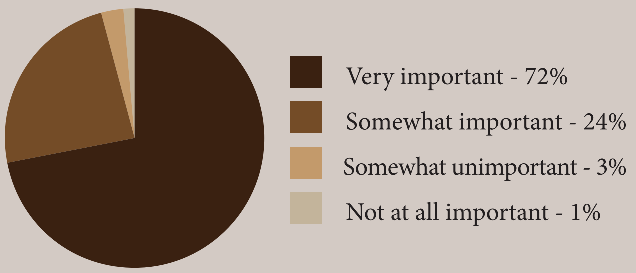


Figure 6: Diverted profits tax

Does the introduction of the UK diverted profits tax undermine UK tax competitiveness?

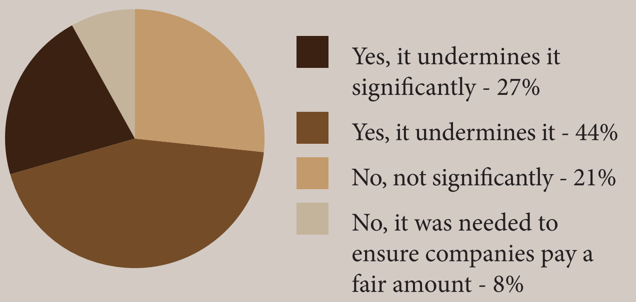


Figure 7: Infrastructure

Does the tax system adequately support infrastructure investment?

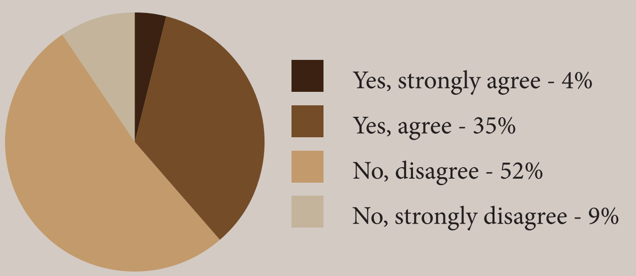


Figure 8: BEPS

The OECD's action plan on BEPS will 'ensure the coherence of corporate income taxation at the international level, restore the intended effects and benefits of international standards, and ensure better transparency and promote increased certainty and predictability' (*OECD BEPS FAQs*). Do you think the outcome will meet those objectives?

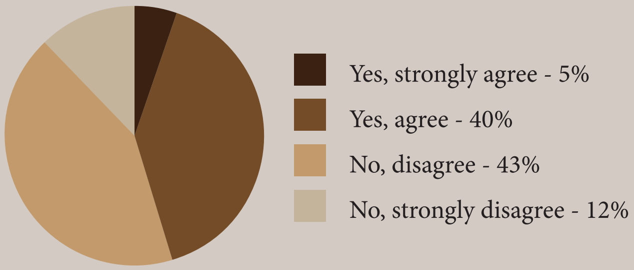


Figure 9: Enforcement

Has the process for resolving disputes got better/worse during the coalition's term in office?

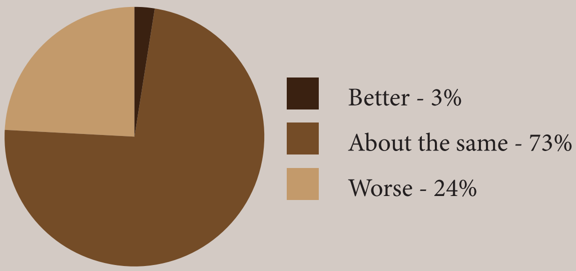


Figure 10: Does HMRC's litigation and settlement strategy work well in practice?

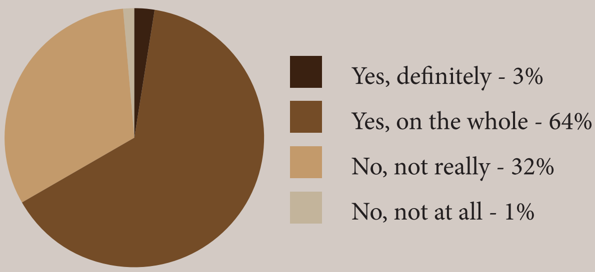
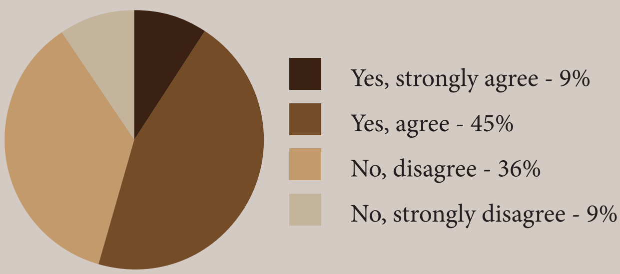


Figure 11: Are accelerated payment notices a good idea?



The OECD need to ensure the tax paid in respect of services/goods provided via digital platforms is fair and consistent. Across all their workstreams they have stupidly chosen the path of looking at profit (a wholly subjective concept) allocation. The sensible, simple and secure route would have been to tax transactions/cash.

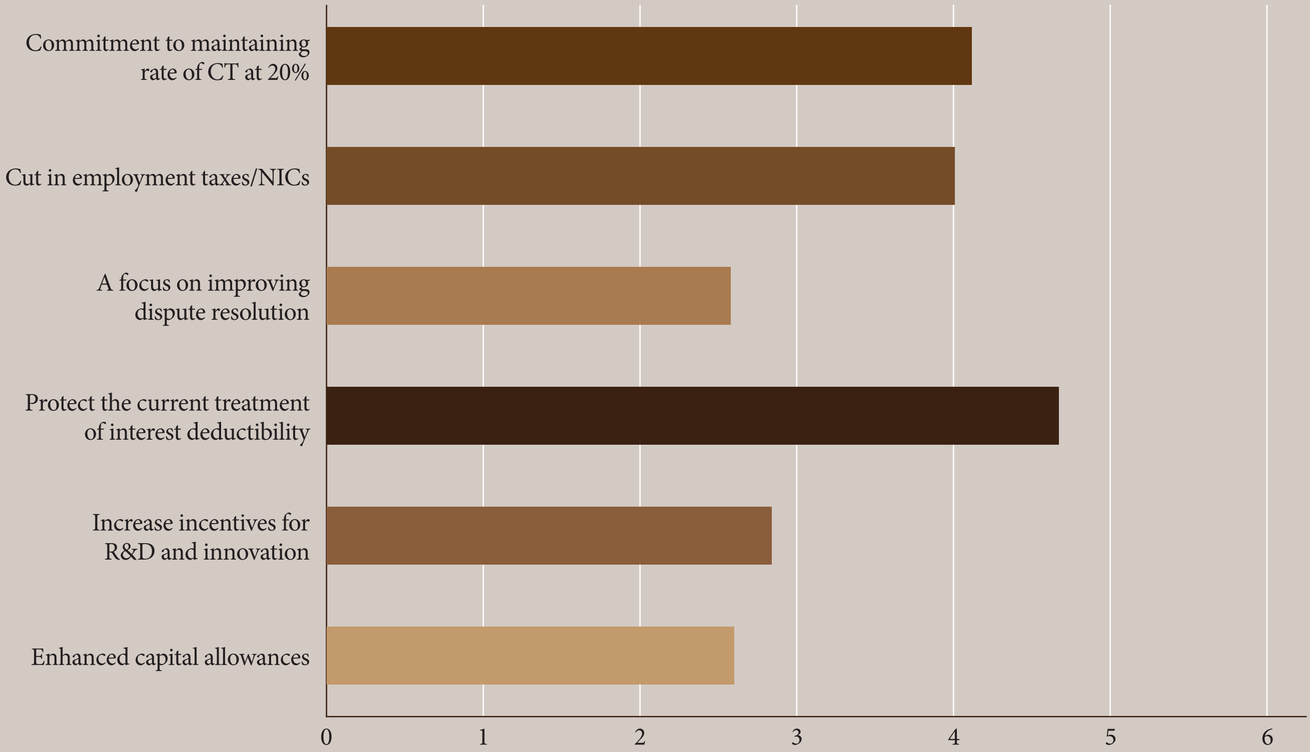
- I do not believe this will be achieved as always national interest will take a front seat.
- Not all territories will implement everything in the same way and at the same time. Some will see it as an opportunity to cash grab hence double tax may arise. Administration will increase significantly. UK diverted profits tax is an example of this.
- Only achievable with widespread international implementation, which seems unlikely in many areas. The UK and other nations jumping the gun with individual new tax policies (e.g. diverted profits tax) also undermines BEPS project.
- Almost all the success of BEPS hangs on the September 2015 deliverables, and I am not convinced that a clear road map will emerge after September.
- BEPS will increase the compliance burden. CbC gives a tax authority an additional tool even where a taxpayer is fully compliant. This will increase, rather than decrease certainty and predictability.
- Given the way that different governments, including the UK on the DPT, have driven ahead with unilateral actions I think there is a real risk of multiple taxation with the consequent reduction in investment as companies try to minimise or mitigate that risk. The increase in uncertainty during the current process is undoubtedly reducing investment and forcing companies to waste time and resources amending structures rather than on productive investment for the future. When the tax system depends on the goodwill of the tax authorities as it now does in the UK you are in a very difficult situation.
- There is a heightened risk of the same profits being taxed in more than one jurisdiction as a result of the action plan.
- By and large, but UK acting unilaterally and others will do the same. The basic premise is ok, the application less so.
- But I would like to see stronger action in parallel to tackle and reduce withholding taxes around the world. Countries that tax transactions should concentrate on indirect taxes.
- It is a marginal 'yes'. There will be better transparency (e.g. country by country reporting), and there is likely to be more confidence by politicians and possibly the public in the international tax system but there will continue to be uncertainties and mismatches in the final outcome.
- There is a risk that the BEPS agenda will introduce uncertainty into the countries that adopt the measures and consequently in the UK could undermine the work done by the current and previous governments on corporation tax reform and the competitiveness agenda.

Advice for a new government

- Restore a measure of tax relief for capital investment in buildings for manufacturing (or indeed building investment generally). IBAs have been abolished and UK has no relief for any building investment (other than under RDA rules). Most other countries at least allow a deduction over time and so UK remains very uncompetitive in this respect.
- Continue with the process of publishing draft legislation as that has worked well. Also try to follow the rules of international law and not unilaterally overrule them. The UKCS leasing rules spring to mind as being particularly inept.
- More predictable – roadmap change.
- Be predictable and don't make major swings in policies for symbolism or vanity projects – only if they will be major tax raising issues should they be considered.
- Retain and expand the OTS. Resource HMRC properly and make it get the basics right. Simplify processes whereby past errors/issues can be disclosed and extra tax paid without complicated refilling or the fear of a heavy-handed reaction.
- Don't increase CT rate.
- Have the courage to follow the sensible recommendations from the Office of Tax Simplification, especially on aligning income tax and NICs.

Priorities

What do you want to see from the next government? We asked respondents to rank the following in order of importance, and we have displayed them accordingly.



- Reissue a roadmap for the next five years and give business a clear direction on tax policy and stick to it.
- Stability, predictability and consultation are essential, and there should be a genuine effort (not the current lip-service) to promote simplification and reduce complexity.
- Keep it low, keep it mandatory!
- Do not forget that HMRC have to operate the policies and need support. Business has high regard for HMRC and it is a critical part of a competitive UK, it would be very damaging to lose this.
- Reconsider the tax environment for the O&G sector operating in the UKCS.
- Focus on simplification of the code rather than anti-avoidance and be bold.
- The OECD targeting of BEPS has highlighted that tax systems and policy should not be portrayed as competitive, it is meaningless and unhelpful. Tax policy should be framed around the concepts of fairness and consistency, not competition. Finally, the UK's infrastructure requires many many £billions spent on it, tax policy needs to reflect this and rebalanced if this country wishes to avoid the chaos that an inadequate infrastructure will create.
- Reduce the number of taxes and simplify the tax base of those remaining.
- Consistency. Have a plan for what to do when the CFC financing exemption goes otherwise multinationals may leave the UK again. Do not rush any BEPS driven changes for the sake of politics. Seek to cut the administrative burden, not increase it.
- Take the politics out of it. Simplicity. Send Margaret Hodge on a course entitled 'if you don't agree with the current legislation, change it' – this is your job and stop throwing stones at corporates for political ends.
- 1. Read my lips – no more taxes! 2. It's the economy stupid! More investment tax incentives for tertiary industries.
- Extend the patent box to other kinds of technology such as Big Data.
- HMRC now has too much power. Only those persons with deep pockets and access to good advice have any hope of getting justice if HMRC turn against you. The law is too complex and in too many places it is dependent on the right 'intention' to get the right result. This makes effects very subjective and very difficult to plan around. Uncertainty is the greatest hinderance to investment.
- Don't introduce new taxes, fix the workings of the ones we already have (e.g. council tax deficiencies, mansion tax...).
- Abandon student loans and the industry that supports them and recognise that most graduates paid for their education through normal taxation on higher salaries generally earned.
- Don't act in haste out of a desire to be seen to be doing something. Consult with relevant stakeholders. Allow the OECD to complete its work on BEPS without taking any further unilateral action. Restore public confidence in HMRC.
- Maintain competitiveness, continue with a roadmap businesses prefer the certainty of knowing what will happen when. Make employing people more attractive, don't raid pensions. Replace business rates with something fairer across business. Work on a simplification agenda. Make the authorities work faster and smarter. Maintain the current cfc regime and interest deduction.
- HMRC needs to be properly resourced, trained and motivated, and needs to be supported at all times by senior management and politicians. Work of the Board's Solicitor needs to be reviewed, as the present impression is that those people are useless.
- Work with the OECD on BEPS rather than knee jerk / political responses to perceived avoidance.
- Seek to significantly reduce complexity and to take a far more radical approach to OTS. Cease pandering to those who through populism seek to divisively politicise tax. State very clearly the case for reducing taxes to make everyone better off. ■