Improving large company tax compliance

Management of taxes | Tax voice



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Jim Wilson examines the approach being taken to large company tax corporate governance.

There have been a number of changes recently to the way in which HMRC is seeking to work with large businesses, in particular with the additional compliance measures published in the draft Finance Bill 2016 which will see an increased scrutiny of tax corporate governance with legislative backing.

The new finance bill measures cover three separate but inter-dependent strands:

- a requirement for large businesses to publish their tax strategy as it relates to UK taxation;
- a framework for co-operative compliance (in place of the voluntary Code of Practice previously proposed);
- a series of 'special measures' designed to discourage persistently high risk behaviour.

HMRC has explained that whilst the existing large business strategy has worked well for the majority of businesses, this needs to be reinforced to deal with those enterprises that have yet to adopt the best practice in tax compliance exhibited by the majority, those who persist with aggressive tax planning, and/or those who resist

full and open engagement with HMRC.

The new provisions will apply to large groups, companies and partnerships, broadly defined as for the Senior Accounting Officer (SAO) regime (aggregated UK group turnover more than £200m, or a balance sheet total more than £2bn in the previous financial year). Groups of companies within the UK country-by-country reporting regulations are also brought within the rules regardless of the UK turnover. This could also bring in smaller UK businesses than the SAO and who may not have an ongoing relationship with HMRC through a customer relationship manager.

Publication of Tax Strategy

There will be a mandatory requirement for large businesses to publish their tax strategy in relation to UK taxation on the internet, making their approach to tax planning and the relationship with HMRC open to the public. The requirement applies to all financial years beginning on or after July 2016. Many large companies already have a tax strategy, but the requirement for this to be published is new.

The tax strategy to be published must set out:

- the approach of the UK group / company / partnership to risk management and governance arrangements in relation to UK taxation;
- their attitude towards tax planning (so far as affecting UK taxation);
- the level of risk in relation to UK taxation they are prepared to accept;
- their approach towards their dealings with HMRC.

Other taxation information may also be included.

The strategy must be owned by the executive board, based on the rationale that increased scrutiny of an organisation’s approach to tax matters by the board discourages aggressive behaviours. HMRC has, however, dropped its previously proposed requirement that the strategy must cover any effective tax rate target.

The strategy must be published before the end of the current financial year and it must be accessible to the public free of charge for at least a year after it is first published. A failure to comply with these requirements, non-publication or incomplete content may lead to a penalty of £7,500.

This requirement is a significant shift in HMRC mandating further transparency which differs from the requirements multinationals will face in other countries. Even with the changes to what was originally proposed in July 2015, this will add a new layer of compliance burdens to all large business, including the vast majority that meet their responsibilities in respect of taxation, with questionable value to HMRC in tax compliance terms.

Framework for Co-operative Compliance

It is proposed that a framework for Co-operative Compliance will be introduced in April 2016 which will provide a set of principles that both large businesses and HMRC should engage and work within. The framework is intended to recognise the value of mutuality between both parties and influences HMRC's approach to risk management – a significant shift in approach compared to the originally proposed voluntary "Code of Practice" which was targeted only at taxpayers.

The draft framework codifies many of the factors which HMRC already takes into account in assessing whether or not a business is low risk, while helpfully setting out more clearly than it has before what business can expect in return. HMRC commitments to respond to queries in a timely fashion, to prioritise work where there is real uncertainty, commercial urgency or absolute risk, and to avoid unnecessarily wide-ranging enquiries are very welcome. A proposed written commitment to an escalation mechanism within HMRC where a reasonable solution cannot be reached through to the HMRC Deputy Director is also valued.

HMRC proposes to consult further on the content of its draft framework in the next few months. We understand that this framework will not be legislated and there will be no requirement for signature.

Special Measures Regime

The government is further legislating that large businesses with an ongoing history of aggressive tax planning and/or refusing to engage with HMRC may be subject to special measures. Businesses will be advised that they may be at risk of this and a twelve month improvement period will allow HMRC and the business to work together to resolve issues. At the end of the period, the business will either have improved and so not enter special measures or be notified of entry into special

measures. At this stage no sanctions are triggered.

Businesses who enter special measures risk sanctions if they demonstrate further instances of the behaviours that led to their inclusions in special measures. Sanctions could include:

- removing access to non-statutory clearances
- removing the defence of ‘reasonable care’ (which will make it easier for HMRC to charge penalties)
- potentially naming as being in special measures.

Two years from entry HMRC will conduct an ‘exit review’ to decide whether the behaviours have improved and the business should exit special measures or whether an extension is required.

The proposed special measures regime is a significant tightening of current sanctions for non-compliance, albeit that it is said to be reserved for a very small number of persistent high risk businesses. The legislation would allow HMRC to bring a business into the special measures regime as a result of an assessment of its tax compliance risk (without necessarily any finding that its returns have been incorrect as a result). Given the significant consequences, it is important that as the detailed operational design of the regime is developed there are appropriate governance arrangements and safeguards.

Conclusion

In light of these proposals, it is clear that there is a new definition of “best practice” emerging with regards to tax governance and transparency and it will be important for all large businesses to start to prepare for these changes early to ensure they are best placed when the legislation is introduced.