



HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ

Julian Heslop
Chairman
The Hundred Group Fiscal Committee
C/o GlaxoSmithKline plc
980 Great West Road
Brentford
Middlesex TW8 9GS

21st July 2008

Dear Julian

Taxation of Foreign Profits

Thank you for your letter of 30 June 2008 relating to the review of the taxation of foreign profits.

In June last year, the Government published a discussion document setting out initial thinking on reforms to the rules for the taxation of foreign profits. It was a response to calls from business to reform the current rules with a move to a dividend exemption. The objectives of any reform must be to enhance the competitiveness of the UK tax system, while protecting tax revenues.



Since the publication of the discussion document, we have had extensive and constructive engagement with business on the detail of these proposals. It is clear that there is still a strong case for a dividend exemption but we are yet to reach agreement on proposals that would minimise the fiscal risk it could imply.

In your letter you suggest it would be possible to proceed with a dividend exemption, perhaps accompanied by a form of debt cap, with minimal fiscal risk, but that other anti-avoidance measures could follow at a later stage if necessary. Although it remains our objective to introduce a dividend exemption, our estimates show that to do so could impose significant costs on the Exchequer.

Based on these estimates, my current view is that the fiscal risks are too great to enable us to introduce a dividend exemption in next year's Finance Bill. However, I know that you have thoughts on this fiscal impact and I would welcome further discussion on the analysis of these costs. This will enable us to come to a better understanding of the associated fiscal risks and work towards a package that would enhance UK competitiveness and meet our objective of revenue neutrality.

It is clear that elements of the changes to Controlled Foreign Companies rules and interest restrictions that were set out in last year's discussion document could cause problems for business, specifically the proposals relating to the CFC rules that would have affected the tax treatment of intellectual property and impacted upon



certain sectors disproportionately. It is my judgement therefore that we should not continue our discussions on the basis of reforms that include these particular elements.

Instead I would like to discuss our position, as set out in the attached technical note, with you and other representatives of business. This will also provide an opportunity to advance the debate on strengthening the competitiveness of the UK's Intellectual Property tax structure.

My officials will be in contact with you and other stakeholders shortly to discuss arrangements for taking this forward. In addition to these discussions, I expect this to form part of the agenda for the next meeting of the Business-Government Forum on Tax and Globalisation.

*Yours
Jane*

RT HON JANE KENNEDY MP