Corporate Tax Reform: Delivering a More Competitive System

Business forum on tax and competitiveness

8 December 2010
Agenda

1. Corporate tax reform: the Government’s aim
2. The Government’s principles for corporate tax reform
3. Policy priorities for the Road Map
4. Interest deductibility
5. CFC reform
6. Innovation and taxation of IP
Corporate Tax Reform: The Government’s aim

The Government’s priority is returning UK economy to balanced, sustainable growth.

“Our tax system was once an asset. And it needs to be an asset again.”

Exchequer Secretary’s foreword, Corporate Tax Road Map

The programme of corporate tax reforms has been designed to restore the UK’s tax competitiveness and provide certainty to business:

• creating the right conditions for business investment and growth;
• responding to business concerns over instability and unpredictability;
• reversing trend of businesses leaving the UK

How far will the Road Map achieve these aims?
The Government’s principles for corporate tax reform:

- **Lowering rates while maintaining the tax base** – A low corporate tax rate with fewer reliefs/allowances will provide the best incentive for business investment

- **Maintaining stability** – A stable tax system is vital to business

- **Being aligned with modern business practice** – The tax system needs to keep pace with global developments and not stifle adaptation or create perverse incentives for business

- **Avoiding complexity** – Simplicity to be a feature of good tax policy, seek to avoid complexity where possible

- **Maintaining a level playing field for taxpayers** – The tax system should be fair across taxpayers without distorting commercial decisions

Do you support these as the right principles? How should we prioritise when trade-offs arise?
Policy priorities for the Road Map

The Government has set out a significant programme of corporate tax reforms to restore the UK’s tax competitiveness. The key announcements are:

- As previously announced, reduction in main rate of corporation tax from 28% to 24% by 2014
- Reform of the CFC rules for 2012 to make them more competitive with CFC interim improvements in 2011
- Introduction of a 10% Patent Box to encourage innovative business to invest in the UK and reaffirming the Government’s commitment to retain and build on the support R&D tax credits provide for innovation, including consideration of the proposals of the Dyson Review
- An opt-in exemption for corporate tax on foreign branch profits

Do you agree that these the priority areas to focus on? Are there other priorities that the Government should be considering?
The Government is ruling out fundamental changes to interest deductibility

• The Government remains committed to interest being relieved as a normal business expense irrespective of where the proceed of the loan are put to use.
  – Changes to interest rules would be disruptive for business
  – Changes could undermine stability and certainty and threatening investment
  – The UK’s current interest rules are considered by businesses as a competitive advantage
  – Difficulty in designing workable rules which are fair to all businesses without creating complexity and uncertainty

The Government therefore must retain some CFC protection for financing to protect the UK tax bases against risk of artificial diversion of profits from the UK.

Do you have any comments on this approach?
CFC reform – taking a more territorial approach

Current rules can go further than is needed to protect UK corporate tax base

Government’s aim is to ensure CFC rules minimise impact on commercial decisions and do not interfere with efficient management of overseas operations, while protecting the UK tax base

Package of interim improvements – including foreign to foreign intra-group trading activities exemption – being taken forward for FB11 as the first step

The document aims to provide business with as much certainty as possible over what Government will deliver on key issues of financing income and IP:

- Partial finance company exemption that could bring a proportion of overseas financing income within UK tax charge depending on how entity is funded.
- IP proposals will be more targeted and flexible by identifying high risk entities that hold IP with a substantial UK connection then assessing whether any profits have been artificially diverted from the UK

Do you have any comments on this approach?
Innovation and taxation of IP

The taxation of IP plays a key role in the Government’s corporate tax ambitions

The Government’s focus is on high-tech and scientific IP given strong link to R&D and other technological activities. Additionally, the majority of businesses hold and derive profits from some form of IP – Government has set a clear direction of prioritising rate reductions, which benefit all businesses, over broadening reliefs.

The Government will introduce a Patent Box – applying a 10% tax rate on profits arising from patents to apply from 1 April 2013 – and will work with business to design a viable relief

The Government reaffirms its commitment to retain and build on the existing R&D tax credit scheme to create the right environment for innovative companies to prosper. The consultation considers whether the current schemes are sufficiently well targeted.

Do you have any comments on this approach?