Large groups' tax departments:
factors that influence tax management

Prepared for HM Revenue & Customs by

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Foreword

HM Revenue & Customs commissioned this study to explore the factors that influence the attitudes, motivations and practices underpinning tax management among the departments' largest business customers. Tax managers' views were sought in order to better understand how the tax function is resourced and organised, attitudes to risk, and how tax planning fits into the group's wider objectives.

The O'Donnell Review, which led to the creation of HM Revenue & Customs in 2005, set three clear objectives for the new department – an improvement in customer focus, an improvement in cost efficiency, and closure of tax gaps.

This study contributes to our ongoing efforts, through consultation and research, to collect the evidence to help us to meet these objectives. Since this research was undertaken, HMRC has published the '2006 Review of Links with Large Business', an appraisal of how we do business with business which looked at what large corporates want from their relationship with the tax authorities. The review, endorsed by business representatives, proposed a framework within which business and HMRC can work together to improve the nature of the relationship. This has already been followed up with two further consultation documents at Budget 2007 – one on delivering the Review of Links and the other on HMRC's approach to compliance risk management for large business – and two in June taking forward specific recommendations of the Review of Links.

One of the main proposals of the Review of Links is that HMRC take the business perspective into account in everything it does. The findings from this small qualitative study with tax managers builds on our growing body of knowledge about the large business perspective, particularly the drivers behind decision making.

I would like to express my gratitude to all those who gave up their time to participate in this research.

Dave Hartnett

Director General (Business), HM Revenue & Customs

Glossary

The following abbreviations occur in this report, especially in material quoted verbatim from interviews.

CRM	Client Relationship Manager – see http://www.hmrc.gov.uk/lbo/operating-model.pdf
CT	Corporation Tax – a tax on a company's taxable income or profits. See http://www.hmrc.gov.uk/businesses/tmacorporate-tax.shtml
ETR	Effective Tax Rate - the working ratio of taxation to profits that might be used within a business. Can be defined differently by different organisations, depending on the basis used.
FD	Finance Director, or Financial Director
IPT	Insurance Premium Tax
LCF	Large Corporates Forum – a consultative panel of tax managers from large businesses and members of HM Revenue & Customs staff. See http://www.hmrc.gov.uk/lbo/lbo6.htm
LBS	Large Business Service – a division within HM Revenue & Customs that deals with the largest businesses, across all the Department's tax regimes. See www.hmrc.gov.uk/lbo/index.htm
MD	Managing Director
NIC	National Insurance Contributions
PAYE	Pay As You Earn
VAT	Value Added Tax

Summary

This qualitative study comprised interviews with the tax managers responsible for Corporation Tax (CT) in 37 large groups in the UK, completed by September 2006. The research was undertaken to understand their approach to CT, and in particular to explore the drivers that shape attitudes and behaviour in CT work.

The study found a wide spectrum of corporate attitudes and practices in CT, ranging from the ‘aggressive’ to ‘risk averse’. The tax managers themselves were comfortable applying these terms to their own policies.

The range of views and practices appeared to result from two main influences. The first of these was differences in corporate styles of management: some companies approach all aspects of their operation in a more risk-averse manner than others. The second was the influence of the individual tax manager within that management style.

Most tax managers said that they and their companies were more reluctant than they used to be to embark on tax planning activities. This reluctance was prompted by, as they saw it, increasingly complex tax rules, the prospect of future reversals, and the increasing risk-aversion of managements as a result.

Key findings were as follows:

Attitudes and drivers in tax

- The tax managers described separate influences from management, shareholders, financial commentators and the tax authorities in shaping how they approach taxation. They were sometimes sceptical of the extent to which these different groups understood tax issues within their business.

- All the companies strove to deliver effective administration of compliance tasks. Good ‘housekeeping’ avoided penalties and pre-empted unnecessary and time-consuming scrutiny by the authorities. It was also the major measurable indicator built into some tax managers’ incentives package.

- Some participants analysed their tax plans and behaviour in terms of risk-management. The subjects for risk management included the company’s finances, now and in the future, and its reputation with customers, shareholders and HM Revenue & Customs. The prime tools for reducing such risks were accuracy in forecasting, making sensible precautionary provisions, and aiming for consistency in effective tax rate (ETR).

- Tax managers distinguished between tax planning in the *structural* and *operational* contexts. Structural tax planning was concerned with capital transactions; operational planning with routine commerce. Structural tax planning was seen as a legitimate area for care and action, while operational planning was regarded as being frowned upon by the authorities and therefore more difficult to sustain.

- Participants said that the 2004 disclosure rule changes, combined with legal decisions and a perceived growth in complexity in the tax rules, made tax avoidance ‘devices’ less attractive and companies more wary of those that promote them. Some also said that the basic rate of Corporation Tax was not so low compared with other countries as it used to be.

Corporation Tax – actual and effective rates

- The actual size of the current annual CT bill varied considerably across these large groups, from zero to a conventional 30 percent or so of profits. Not every group paid specific attention to their Effective Tax Rate (ETR) and of these not all set a 'target' for ETR. Very few were trying to manage ETR downward as a strategic aim. This is partly because the ETR is considerably different from the actual tax that many of these groups were paying, and partly because several of them felt that ETR was beyond their power to influence significantly.

Tax Departments – structures and activities

- Tax managers in these groups had two principal roles: management control and reporting of tax affairs; and strategic input to company plans and decision-making.

- It was usually difficult, and often not possible, for tax managers to identify a specific sum that embraced all the costs of administering and handling Corporation Tax in their business. For some, such costs varied considerably from year to year, as specialists were brought in for advice on acquisitions or other structural changes.

- Most companies interviewed used outsourcing to assist with CT work. The pattern of such outsourcing was diverse: some kept most routine work in-house, while others look for global outsourcing partners to handle compliance.

- Tax managers were not apparently in receipt of bonuses or incentives that depended on their performance in cutting company tax bills. Rather, such bonuses, if awarded, were for meeting targets in terms of timings and service to internal 'customers'.

Working relationships with HM Revenue & Customs

- Working relationships with HM Revenue & Customs were generally regarded as effective, and tax managers saw changes in the Large Business Service as potentially beneficial.

- Companies wanted to be seen as candid and open in their dealings with the department, and to foster a good working relationship on that basis. But several also stated that they would be ready to defend themselves vigorously against challenges from HM Revenue & Customs, if challenged over their interpretation of the rules.

1 Introduction

1.1 Background

The largest corporate groups are businesses that often operate in many centres around the world, under a range of tax regimes. Most of the leading corporates active in the UK are multinational in their operations. Many, indeed, are incorporated overseas (in the USA for example, or elsewhere in the European Union). The multinational perspective in such organisations has a profound influence on many strategic decisions that they take about business locations, and the sourcing of materials, of production, and of services.

HM Revenue & Customs recognises the distinct circumstances, needs and service requirements of these large groups, by dealing with such companies through a special structure – the Large Business Service (LBS). These needs and circumstances further addressed within HM Revenue & Customs though a range of working groups and practices, including the existence of LBS Client Relationship Managers (CRMs). The CRM is the single responsible, accountable person who takes ownership of risks across all taxes for their customers.

HM Revenue & Customs has also fostered a strong working relationship with the 'community' of large business groups through its leadership in the Large Corporates Forum (LCF). This group meets three times a year, and in 2006 had attendees from 27 corporate members in the UK.

This study focused on CT, except where comparisons or contrasts between taxes helped a tax manager to explain a point. It should be acknowledged though that a typical tax department may have responsibility for a range of other taxes including VAT, IPT, PAYE, NIC and others, which have different tax planning behaviours and opportunities.

1.2 Research aims

The overall aim of this research was to identify and explore the factors that influence large firms' Corporation Tax management, from the perspective of the tax manager.

The study will complement analysis of the subject from the viewpoints of other stakeholders and other groups of taxpayers. Tax managers' propensity to reduce the tax charge might be diminished by a series of 'principal-agent' relationships (such as those between shareholders and managers); and by the difficulty of setting effective incentives in a context where performance is difficult to measure. A key issue for the research was therefore to explore the incentives on senior tax managers, and to test how far these drive Groups' tax management.

1.3 Research objectives and scope

The research objectives were: –

- To determine how the tax function is resourced and organised in a selection of large businesses in the UK;
- To explore the attitudes, motivations and practices underpinning the Corporation Tax management of these large businesses;
- To suggest explanations for variation (of attitudes or practices) between companies; and
- To help HM Revenue & Customs anticipate how large groups will respond to changes in the tax environment including
  - policy changes;
  - vulnerabilities in the law that are created by, for example, court decisions;
  - changes to the law that create new tax planning opportunities
  - legislation to close so-called 'loopholes'.

To provide insights into how these large groups manage their affairs with regard to CT, the study gathered information on the following aspects: –

- A structural description of the group's tax department,
- A picture of the organisational dynamics of that department,
- A description of the group's attitude to risk, in tax and other management areas,
- A view of the group's wider objectives,
- The group's-eye view of its relationship with the tax authorities, and
- The level and source of information about the latest tax planning schemes.

1.4 Research method

The exploratory nature of the objectives demanded a qualitative research approach. The expected variation between companies in their attitudes, priorities and practices meant it was essential that they be interviewed singly. And because of the potentially sensitive nature of the subject matter, all interviewing was carried out in person at the participants' premises.

This report conveys the findings from a total of 37 face-to-face interviews with tax managers drawn from large corporate groups. The research investigators themselves made all appointments for interviews, and each of the four members of the interviewing team was a senior business interviewer, with extensive experience in and aptitude for interviewing at a senior executive level.

The successive stages of the data collection process are described below. Details of the conversion rates and other technical parameters are shown in the Technical Appendix (Appendix A) of this report.

The agreed target was to achieve 35 completed interviews, in two stages – an initial feasibility test, comprising five interviews; and a later ‘main stage’ with a further 30 interviews. HM Revenue & Customs supplied the research agency with a list of businesses that fall within the scope of its Large Business Service. FDS telephone interviewers supplemented that list with any missing contact information for the listed companies. The manager co-ordinating the research at HM Revenue & Customs then wrote to each candidate for interview. The notification letter (shown in Appendix B) set out to: –

- explain the nature of the forthcoming study,
- describe what might be asked of participants,
- give an assurance of total anonymity and confidentiality,
- offer a means by which tax managers could find out more about the study (from the research agency or from HM Revenue & Customs), and
- offer candidates a method of opting out of further contact if they chose not to take part.

At the same time, the CRM for each company in the list was informed of the research, in case of any queries about it arising from the companies involved.

Across the study as a whole (including its feasibility stage) the notification letter was sent to 148 people. Of these, 45 declined to take part. Among the remaining 103 available candidates, some were unable to commit to an appointment (because of annual leave or other commercial pressures), but the list was more than sufficient to secure the 37 interviews reported here.

Members of the interviewing team approached candidates (by telephone or email) to seek appointments. The interviewers then visited respondents at their place of work for interviews lasting between 60 and 90 minutes.

The interviews were exploratory in nature, and used a topic guide (shown in Appendix C), which covered three main subject areas: –

- The individual and the department
  - how the group structures itself (and funds itself) to handle its CT responsibilities
- The focus in tax management
  - the priorities and pressures that determine tax practice within the group
- The work
  - how the manager and department performs or allocates its functions
  - including consideration of its working relationship with HM Revenue & Customs

The first five interviews took place between 10 and 20 January 2006. The subsequent 32 ‘main stage’ interviews happened between 13 July and 6 September 2006. All interviews were tape-recorded, and full transcripts were produced for analysis.

A key component in the research was that those taking part should remain anonymous, to ensure an open and frank exchange of ideas and information. This had several consequences for this report: –

- Any figures quoted (for example, a company's turnover or profit) are reported in deliberately broad bands

- Businesses are referred to using five broad 'super-sectors': –

    – Infrastructure (inc. construction, transport, energy)
    – Manufacture
    – Business services
    – Financial services
    – Retail.

Direct quotations from the interview transcripts have in some examples been altered slightly, to maintain anonymity. In most cases quotations are attributed to a specific interview numbered according to the scheme shown in Appendix A.

1.5 Qualitative research – a caveat

These findings illustrate the differing ways that individuals, companies or business sectors can think, feel and behave, without attempting to gauge the relative prevalence of differing views or perceptions. The sample interviewed in this study was not chosen as a representative sample. Instead, care was taken to ensure the sample for this study was inclusive – that is, selected so that the business base was broadly covered, including tax managers drawn from a wide range of business types (and sizes).

It is possible, but unlikely, that there exists among 'large groups' a widespread body of opinion that was not met in this study. For example (and obviously), no views were obtained from those not interviewed. It is reasonable to suppose that the groups with the most ambitious tax planning strategies were also the least interested in being interviewed, and that this study has simply omitted them for lack of access and cooperation. However, there was a broad spectrum of views and behaviour found among those who took part – ranging from the risk-averse through the complacent to a few deliberately tax-aggressive businesses.

The findings from this study should not be interpreted numerically – it is dangerous to infer conclusions about 'majority' views or 'prevailing' attitudes from this form of research. Being based on only 37 interviews, these findings should not be used as the basis for inferring generalisations about large businesses.

2 Attitudes and drivers in tax planning

2.1 Tax focus and strategy

Some groups had defined and formally documented their strategy in tax, setting out their policy and aims, and the methods by which they will achieve them. More commonly, it seemed, tax policies were discussed and agreed between the tax manager and the Board, but there was no formal documentation of them as such.

Some companies had a formal Tax Strategy or Tax Policy, which had received board approval and was regarded as one of the cornerstones of the tax department's work. Where tax policy was documented, the written record would specify a range of protocols beyond the company's attitude to tax. It covered (in different formulations) any of the following: –

- Demarcation of internal and outsourced functions
- Personnel policy
- Approach to tax risk
- Taxation objectives.

> *We have a Group Tax Policy, which I drafted and agreed with the FD, and then that was approved by the board last year ... The aim is that it will be updated every year, so I need to do it again soon ... It's very broad. Over time I think it will become more detailed. It sets up what we do, that we outsource certain work and we do other stuff in house. It says that we aim to have high calibre staff, and that we will use external advisors as appropriate. So we'll try and do most stuff in house. And it also sets up our risk approach.* (Interview 21, infrastructure)

> *We have a Tax Risk Management Policy, and we insist on making sure we review everything, any new product, any new transaction, any new business line. Everything has to be reviewed by the tax department. So there might be something that might go to the risk committee, we'll have to review it first; and the requirement is there because we don't want any tax risk materialising in the future and creating liability for us*. (Interview 19, financial services)

Possession of a formally documented policy was not obviously associated with other corporate characteristics – such as the size or nature of the business. Rather, it seemed to depend more on the Board's (or tax manager's own) outlook and management 'philosophy'.

In this sample, the companies with such a document were unusual. More often, the policy could be described, but did not exist as such on paper.

> *We have discussions, but it's not formalised as such. We have general discussions and meetings about various issues, and where we want to go, and what we want to do.* (Interview C, Infrastructure)

Notwithstanding the lack of a documented strategy, as noted in the following section, all tax managers found it easy to describe their company's priorities in dealing with CT.

2.2 Tax priorities

Companies differed in terms of the degree of 'aggression' with which they approached CT (and other taxes). Some were more ambitious than others in wanting to minimise their tax liability, and more prepared to adopt mechanisms for achieving this. A few (three in our sample of 37) were unwilling to discuss their approach to tax planning at all.

All companies strove to deliver effective administration of the compliance tasks; the more sophisticated also further analyse their tax plans and behaviour in terms of risk-management.

The subjects for risk management include (with varying priorities) the company's finances, now and in future, and also its reputation with customers, shareholders and HM Revenue & Customs.

Whether their group's tax policy was formally documented or not, all tax managers found it easy to articulate a set of corporate priorities in dealing with tax in general, and CT in particular.

The priorities that companies subscribed to usually included the following main requirements: –

- Safeguard the value of the business
- Produce accurate forecasts of business results
- Pay tax on time
- Submit tax computations on time and acceptably
- Avoid auditor changes to accounts
- Make sure any legitimate claims and elections have been taken.

These were the widely-voiced aims, although their rank ordering would differ from one tax manager (and group) to the next, and some would use different words to describe the last in the list – preferring to express this as 'pay no more tax than necessary'. Some also referred to "responsibilities" in the sense of corporate responsibility as underlying their priorities.

A consistent theme expressed by the tax managers was the imperative to 'avoid surprises', whether for management, for City commentators or for shareholders.
So consistency of tax performance (from year to year) was for many an over-riding criterion, whether in terms of the 'housekeeping' required for compliance, or the actual liability for tax.

The six priorities listed above can be divided into two classes – those that are about administrative effectiveness, and those that are risk-based.

Table 2.2 Companies' main aims in tax strategy

Administrative aims	Risk-based aims
• Produce accurate forecasts of business results • Pay tax on time • Submit tax computations on time and acceptably • Avoid auditor changes to accounts	• Safeguard the value of the business • Make sure any legitimate claims and elections have been taken

Every company professed an interest in the 'administrative' targets, if only because to fail to meet deadlines for submission of Returns or payments would attract unwelcome attention from tax authorities. It will also be shown (in section 4.7, page 42) that delivering this administrative performance was the basis of bonuses and incentives for some tax managers, and perhaps their teams.

> ***[What are your tax objectives?]*** *Pay on time. That's about it really, to be honest. Avoid fines, pay it on time.* (Interview 16 - retailer)

> *My main objective personally is to get the CT agreed as early as possible in the year, to get them signed off and then to get them filed with the HMRC.* ***[And why as early as possible?]*** *Because our year end is [month], and historically we've let them really drag on – which is no good for us and it's no good for the [external practice].* (Interview E, infrastructure)

As the quotes below illustrate, the administrative performance of the tax department was often not the only consideration, and indeed could be seen as subordinate to other aims. In this context, some companies also took into account their Effective Tax Rate (ETR) – which almost all defined as the ratio of CT paid to pre-tax profits, both figures being those that are publicly quoted (in annual reports) rather than the actual cash sums in a particular year. In practice, companies tended to pay more attention to the actual cash tax payments required than to the ETR. This is a distinction covered in more detail later, in section 3.2, page 28.

> *The main objective is to manage the CT affairs of the firm effectively. At its very core is making sure that we prepare and file tax returns on a timely basis, pay our tax due on a timely basis and ensure that the affairs of the firm are conducted as efficiently as is possible.* ***[How much importance does your business attach to the effective tax rate?]*** *I'll answer the question with a question. What do you mean by effective tax rate? UK cash tax? That's certainly what HMRC are concerned about. It's not particularly important for technical reasons. We get taxed on a global basis, so the actual cash tax we pay out the door in the UK is not really something which we particularly worry too much about.* (Interview 26, financial services)

> *Our overriding aim is to minimise our tax bill, but then obviously we have a whole lot of things that sit below that – we would avoid the use of artificial tax structure, we would aim to minimise our tax bill by maximising the use of good commercial drivers, those kind of things. So we have clear guidelines ... Each year we set out what's our aim for our tax rate, what do we forecast our cash tax payments globally to be for the year, what projects are we going to implement in the year, what do we intend to do... So that will form what we call our 'performance promise' for the year, and will be 20 items, say.* (Interview 32, manufacture)

The more sophisticated groups (those with greater multinational exposure, and a highly-developed management approach) tended to cite *risk-avoidance* as the way to deliver the consistency that was desirable, and described risks in terms of corporate value and tax-saving, alongside considerations of administrative housekeeping.

The risk categories that tax managers talked about were essentially two: –

- Risk to *value*
    - including jeopardy to the reputation of the company and its brand values; and

- Financial risk
    - including the danger of unforeseen demands from tax authorities at a later date.

Both of these are related to the company's desire to control the amount of tax it pays. Tax managers expressed this control-aim in various ways, each subtly different in nuance.

- To pay as little tax as *possible* ‘Aggressive’
- To pay as little tax as *necessary*
- To pay the *right* amount of tax
- To pay a *fair* amount of tax ‘Conservative’

Perhaps it needs stating that none of these companies expressed a wish to pay *more* tax than they were bound to. The objectives above span and define the spectrum that was found in companies' aims, from ‘aggressive’ (at the top) to ‘conservative’ (at the bottom), and most tax managers were comfortable using the dimension from ‘aggressive’ to ‘conservative’ to describe their own preferences and practices. The following quotations exemplify tax managers' (and groups') positions, ranging in sequence from the more aggressive to the more conservative.

The first examples show the different approach to risk that seemed to be adopted by two groups where the major shareholding was in the hands of either a founder-manager, or a single major shareholder: –

> ***[Where and by whom are the key decisions taken about CT affairs for the UK?]*** *It depends. If it was something on compliance, it would be the FD. If it was something of a high level, let's say tax minimisation, it would probably be [the chairman] ultimately, because it is his company, it's very much his baby ... We tend to look at [CT, in terms of] how much it is in* cash*. That's probably why we've changed our advisers, in the sense that we were probably not minimising it enough, not proactively managing the tax charge.* (Interview E, Infrastructure*)*
>
> *Our principal shareholder has always been more interested in the bottom line – after tax. Most other people – unfortunately particularly the analysts – merely look at the top line. So tax is no part of it. I mean one of the things years ago we used to do is to enter into various schemes which frequently reduced top line profits but increased below the line. Now we wouldn't do that today, because the analysts come first in the queue. But yes, we want to try to reduce our overall tax bill as far as we can. And one of the many ways we do it is by structuring the group sensibly, rather than entering into schemes.'* (Interview 8, financial services)

Adopting a more 'aggressive' approach was not confined to companies with few shareholders. Some others with more widespread ownership (and more frequently-traded shares) also showed similar views: –

> ***[On a tax spectrum from conservative to aggressive, where would you place yourselves?]*** *I think we would be towards the aggressive end. We're not ultra aggressive, but we work hard at it rather than just accepting that it's 30 per cent of everything that we make.* ***[How does the group balance minimising tax cost versus minimising tax risk?]*** *That's very important, because you can be right at that aggressive end and also risky, you don't know where you stand at all. The risk has got to be liveable. The risk is probably more important than the cost, so we wouldn't go to the [position where] we've mitigated all our tax away, but actually it leaves a difficult position. And why do we say that? It's probably three reasons ... First, we're professional people and we're qualified and we've got standards which I like to think that we live up to. Secondly we've got a shareholder face with public people and therefore if you're saying there's no tax to pay, and then in 2 years' time you find there is a lot to pay, that's not just uncomfortable, that's misleading the market – and you're into lots of sanctions which are not comfortable. And thirdly, the Board here owns 25 per cent of this company, so getting it right, we get 25 per cent of what's right – and equally we get 25 per cent of what's wrong.* (Interview 27, business services)

That respondent (and the next quoted) made the important point that even within an aggressive policy, risk management is vital, to distinguish between those tax-saving actions that present acceptable risks and those that are more dangerous.

> ***[Would you say that you're an ambitious company when it comes to tax?]*** *We're not going to bet the house on the basis of saving a dollar. ... We view ourselves as a long-term investor in all the countries where we do business ... We will pay what we think is a correct interpretation of the law; we will pay our tax accordingly. If that means that occasionally we have a dispute or disagreement, so be it.* (Interview 30, manufacturer)

Moving along the scale toward a more 'conservative' position, another set of companies tended to talk of paying the 'right' or 'fair' amount of tax: –

> *The first goal for the department is to make sure we're compliant with all our responsibilities. And then second, behind that but almost on an equal footing, is to make sure we pay a fair amount of tax or the right amount of tax. Pay as little as possible, within the rules. [****But with a very high regard for rules?]*** *Yes. The view has always been, and this has filtered down from the Board, that we need to be able to say that we're paying a fair amount of tax. So we're not necessarily going to be interested in minimising our tax liability to the greatest extent that we can, but on the other hand we're not going just to write a cheque for millions more than we need to. We need to be seen to be paying, I guess, a fair amount.* (Interview 23, financial services)

Other groups expressed the view that in tax – as in other matters – they were risk-averse by nature. This led them to adopt a more conservative position in tax planning, and this meant, for example, that they resisted opportunities that were offered them by outsiders: –

> *The objective set for the organisation on a global basis is to drive shareholder value, generate quality earnings. Now what does that actually mean? Well it means that you give effective tax advice, that you take a balanced approach to revenues and risk, and that ultimately your decisions should generate these quality earnings and not just something that's here today gone away tomorrow. So as an institution we are relatively risk averse. But obviously you have to be business friendly. I think that we're not among those institutions that are into tax-structured transactions, in a way that would be perceived as 'aggressive'. A lot of people have tried to sell a lot of this to us over a long period of time, but it's not something that we have ever really engaged in, in any material way.* ***[Why is that?]*** *You might say it's attributable to me, to some extent. It's attributable to the attitude of the organisation. It's the way the group measures risk and measures reputation. And also you know there's a lot you can do which has the same impact without the same level of risk.'* (Interview 10 - financial services)

The excerpt above shows that risk aversion was not confined to considerations of financial risk. Some tax managers also couched their risk assessment in terms of potential damage to their company's reputation (and hence share value): –

> *What [the company] wants is sustainability. It doesn't want big shocks, but it also wants to push [tax] as low as it can. But it wants to do that in a way that its board and senior finance people feel is, I wouldn't use the word 'ethical' but I think it's appropriate for an organisation of our standing and stature and size ... there are also [companies] that are very aggressive, that do aggressive quick schemes which we don't engage in.* (Interview 32, manufacturer)

> *We do what we can but we don't want to be too aggressive.* ***[So where would you see yourself on a spectrum from conservative towards aggressive?].*** *I would say we're well towards the conservative. I guess we don't particularly want to open ourselves up to scrutiny, and we don't particularly want to attract any adverse publicity ... we're slightly conscious of the fact that if we try to do anything that was on the more aggressive end of the scale then it might open us up to public scrutiny as well. And to that extent we just want to really play it safe and honest.* (Interview 3, business services)

On the basis of this sample, it seemed that some of the more aggressive companies were also those with fewer shareholders, especially where senior management was also a major shareholder; and that the most risk-averse tended to be organisations with a 'household name' quality, which placed a more explicit value on their public reputation. But there may have been exceptions to this, including two well-known and publicly-traded companies that declined to go into any detailed discussion of their approach to tax planning. It might be that they were among the most 'aggressive' in the sample, but this cannot be known.

2.2.1 Managing financial risk

Tax managers addressed and sought to minimise the risks to finance, and especially to cashflow, both currently and in the future. Their tools for doing this were accuracy in forecasting, making sensible precautionary provisions, and aiming for consistency in effective tax rate (ETR).

Managing financial risk included controlling exposure to future liability, but also good housekeeping practices.

> *If you ask my boss what would you like see done, he'd like to see returns agreed on a timely basis and the group's cash tax cash outflow minimised. Obviously we're quite a debt laden business and obviously £1 million sitting in the Revenue's coffers is better in the business.'* (Interview D - retailer)

Controlling financial risk led one company to make deliberate overpayments, to give some protection against the unexpected: –

> *We have to estimate what our tax and profit's going to be through the year, so we have a little model, my forecasting model, showing where profit's going to be when I make my payment. Then I'll update that ... We pay our quarterly payments on account on the due dates. When I'm making my payments on account I will use 30.5 per cent as an effective rate, and I will also put in a small contingency as well, so let's say our profits for the year are predicted at £4 million, I'll put £400,000 of contingency and I'll put £4.4 million in, and pay tax on that basis.* (Interview 24 - manufacturer)

A more general view was that risk-reduction entailed taking a balanced view of exposure, and weighing up the value of present gains against potential future 'surprise' liabilities: –

> *A well managed tax department will, in a sense, take on tax exposure up to the point at which its management feel it's got enough exposure, and that will enable it to generate enough value-added. What it wants to avoid is unintended exposure, or unintended outcomes. So, to put that in to more practical words, we would want to do some tax planning, which could potentially be unpicked by Revenue authorities, so we're taking on exposure. But we do that knowingly, and with a predictable amount of exposure, and on a basis which is honest and responsible and appropriate. Nevertheless, we want to take on exposure up to an amount that is acceptable to the board. What we want to avoid at all costs is unexpected surprises, being attacked on things that we thought were secure or being attacked on errors or finding that we've made arithmetic or compliance errors in our tax returns. That sort of exposure is wholly undesirable.* (Interview 20, business services)

2.2.2 Managing risk to reputation

Tax managers in some businesses are also conscious of the risk to reputation, whether with customers or the broader public, that could be posed by certain types of tax activity.

It was common among these interviews for tax managers to acknowledge, as an inhibitory factor, the reputation that the business (and its people) holds with customers, shareholders and the broad public: –

> *We had a lot of discussion at the end of last year about holding overseas investments, and how should we do that, and financing and so on. We discussed some ideas which [external advisers] said are quite standard, and we said, 'Well, I don't really think it would fit with our clients, our public sector clients, because we don't really want to go in for double-dip financing arrangements.' I always think of the 'Private Eye test'. What would it look like if it was written up there?* (Interview 21, infrastructure)

> *I think, as a person and as a professional, that it is perfectly legitimate to arrange your affairs in a way which happens to minimise the amount of tax you pay. But I think there's reputation risk. And to be blunt, I think that's the reputation of the corporation but also of the directors. And they don't want to be associated with schemes or with reporting that is bad for our reputation and for their reputation.* (Interview A, business service)

The company's reputation with the HM Revenue & Customs was also a factor that some paid considerable attention to: –

> *We shy away from doing anything in the group that would put us on the radar, as it were. If you were to speak to the Revenue or Customs & Excise, I'm sure they would see us as being 'a compliant tax payer' not involved in implementing aggressive tax planning schemes – except for the card-handling fee scheme. We had to do this because our competitors were doing it, and we had to remain competitive.* (Interview D, retailer)

2.3 Areas for tax action: structural and operational

Tax managers usually distinguished between tax planning in two different contexts – structural and operational. The former is concerned with how companies are set up, and how they go about structural changes such as major acquisitions, overseas start-ups etc. The latter is concerned with how they carry on their regular business, within the UK and internationally.

A fairly general view emerged, which was that tax planning in the structural context was a legitimate area for care and action, while tax planning centred on day-to-day transactions was increasingly frowned upon by the authorities and more difficult to sustain.

In talking about their freedom of action or strategy in tax planning, several tax managers were keen to draw a distinction between the *structural* and *operational* domains.

Tax planning in the *structural* sense meant taking account of the different consequences for taxation of alternative ways of structuring companies and subsidiaries (in the UK or overseas); or of acquiring new businesses or properties.

Tax planning in the *operational* sense meant organising the ways the company does its business, with itself or outsiders, in such a way that the throughputs attract lower taxation.

Those two domains for tax planning were regarded as distinct, although there is the potential for some overlap between them. For example, a structural tax planning solution might define a particular relationship between parts of a group, which in turn reduced the liability to tax on profits from intra-company trading.

The view among these managers was that *structural* tax planning is more generally permissible under tax law, and therefore that in taking care to minimise future taxation by adopting particular structural solutions, they are doing no more than the law allows.

> *I'm on a board committee that handles property deals. Obviously there are tax implications in doing those, so tax is brought in at an early stage on all transactions that we do; so it's not that we have a deal and then say afterwards, 'Oh we must think about what we have to do for tax'.* (Interview D, retail)

> *Any business change – business development, any acquisitions, disposals, changes in lease structures, significant changes in the way the trading so moving, maybe moving from using a third party to bringing an in-house distribution company, creating a branch – all of that requires tax sign-off, and most of that would require somebody from my team to get involved in the project. (Interview 32, manufacture)*

Since 2004, UK law has changed to require disclosure of any company's involvement with certain defined 'notifiable' tax planning strategies. Some managers saw the new disclosure rules as having shifted the emphasis in tax planning, from operational to structural considerations: –

> *In our case, almost none of that [tax planning] is on the traditional kind of tax avoidance level. Almost all of it is in support of business transactions which are complex, and on which we need to get definitive tax advice before we can go forward ... [This company] would never undertake anything on the basis that we'll do it in the hope that revenue authorities don't find out about it, and will always do everything on the basis of full disclosure ... so in some respects the disclosure regime itself hasn't changed a great deal ... But I think it has also meant the law companies are looking at different kinds of opportunities. So companies are perhaps looking even harder [at] whether they've structured their business in the most tax efficient way, in terms of putting activities in the lower tax countries. ... One could look in the press and see all sorts of interesting cases ... there are lots of examples of companies which have moved divisions or units around in order to try to have a more competitive tax rating.* (Interview 20, business services)

This awareness – of tax-motivated structural changes by several large and well-known companies – was repeated by several other respondents, and had a bearing (among multinationals) on their views of the competitiveness of the UK. This subject is covered in more detail in section 2.7, page 25.

Structural tax advice was regarded as secondary or subordinate to the commercial considerations involved. In other words, in choosing between alternatives that are equally acceptable commercially, the tax criteria could decide the matter. But tax managers typically said that tax considerations should not predominate over what makes commercial sense: –

> *We don't tend to go for tax 'schemes', for want of a better word, that don't fit with our business model. The business model comes first, and then if we can do that in a tax efficient way we will always try to do that. First and foremost we are a trading operation ... each of our businesses has a high degree of self-determination. They will decide what they're going to do. And tax will come along and try to make sure that what they're doing is done in the most efficient way ... But if we know, for instance, that the business is making an acquisition, they would always share with us that that was what they were doing before they signed up and we would make sure that tax was taken into account. But they wouldn't go out and buy a business just so that we could do a tax scheme.* (Interview 6, infrastructure)

> *We start with what the commercial people want to do. For example when we were looking at setting up our [named country] operations, we did a huge amount of work on whether we should set up an office, or a branch, or a subsidiary. There was some discussion around the benefits of branch or company for commercial reasons, and we said well actually for tax it would be hugely preferable to have a branch. But if you say that's unacceptable commercially, then we'll just have to live with it ... We tried to steer the commercial people into setting up a branch initially, but they were happy to do that. We found a way that gave them what they needed commercially but was beneficial to tax.* (Interview 21, infrastructure)

But even in the area of structural tax planning, some companies felt sensitive to future risks: –

> *We have implemented some schemes in the past that we think are legitimate and valid but it's yet to be seen whether HMRC takes a different view on that.* ***[You haven't had feedback from HM Revenue and Customs on these?]*** *That's right. It's pending, because they do it on a financial year. There's one structure we put in place, legitimate proper financing in the US. The law changed in March of this year, so it remains to be seen whether they will challenge retrospectively.* (Interview A, business services)

2.4 The impact of disclosure rules

The 2004 disclosure rule changes have made tax avoidance devices less attractive and companies more wary of those that promote them

A view commonly expressed by tax managers was that companies' interest in tax planning stratagems in the operational sphere had fallen over recent years, for two reasons: –

- Rule changes and expressed Government policy have made them unattractive, or likely to be challenged before they accrue benefits, and
- Their own or other companies' past or recent involvement with VAT schemes (for example) has increased their caution or scepticism about eventual benefits.

> *I think the disclosure regime has obviously impacted on some people. But [also] we come from a period where we were a very complex organisation to being now a very simple organisation, and there's not really the inclination to get involved in those kinds of structures. So whilst we have done structures which in the past would have been discloseable had the disclosure regime been in force (and one of those is still open with the Revenue) it predates me, and we haven't done anything of that sort since.* (Interview 1, business service)

> *Basically our board do not want to go into tax planning schemes.* ***[Why is that?]*** *Between you and me, I don't think they understand them. Also, in the last two years we have done two schemes on VAT, and we've been bitten and that's put our board off from doing anything in the future ... To be fair, most of the schemes tend to go with property and as we haven't got that much property, there's little that we can currently do to minimise the tax.* (Interview 14, retailer)

> *I'm not tasked to suppress our tax rate, but that's not to say that if someone came up with a way of financing our group that happened to reduce our tax rate that we wouldn't go for it; although I think our appetite for that is less now than it might have been a few years ago.* (Interview A, business service)

2.5 Influences on tax policies

Tax managers were aware of the separate influences of management, shareholders, financial commentators and the authorities as stakeholders in how they approach taxation, and saw each of these as pulling in its own direction. They were sometimes sceptical of the extent of understanding these different groups show of tax within their business.

Analysts and commentators were generally felt to be a more important 'public' than shareholders themselves.

> *I'm not interested in the broader public. I mean it's our shareholders, but the ones that matter are the analysts, because they comment on us and people investing in us. The Revenue [too], because obviously we've got to do our compliance work and pay our taxes like good citizens; and the Board, because the Board need to know what's going on.* (Interview 25, retail)

The group's management could be felt to be the 'voice of the shareholders' because of the duties implicit in their position.

> *Our instructions come from our Group Finance Director, who himself follows the lead of the board, who are alive to the wishes of the shareholders. So that's really how it works. But I think most large companies recognise their responsibilities to the shareholders and to other stakeholders, including the customers, suppliers, staff, governments, and society in general; and I would personally take the view that we do have certain responsibilities to the government and to society in general, and we fulfil those by being honest and responsible corporate taxpayers.* (Interview 20, business services)

In some financial services businesses, a specific wing of the company was itself devoted to finding and deploying structured finance arrangements that are designed to save tax for their clients. These functionaries could tend to pull their own company toward such solutions too, to the extent that one group's tax manager had found himself or herself reining back against an internal pressure that was more adventurous than they were comfortable with.

On the other hand, a tax manager could feel that their own senior management was somewhat overly-conservative, and that more could be done legitimately to reduce their tax bills: –

> ***[Do you feel that as tax manager you are reining people back from more ambitious aspirations?]*** *I'd say that it's more the other way. I point out that tax isn't as dangerous as they might think it might be. This used to be a very, very risk averse organisation, and it has moved away from that position slightly, and that's across the board, including tax. It used not to be middle of the road. It used to be completely the opposite end of the spectrum ... We have done 'ruses and schemes', yes – in (a) a very managed way and (b) a very limited way. They would be entirely financing arrangements – internally, involving the internal structure, so it's about the flow of debt between the companies ... being a UK-based organisation really limits the amount of zany ideas.* (Interview 31 - infrastructure)

Tax departments generally wanted to cultivate a favourable perception and relationship with the tax authorities. But several made the point that this would not mean passive acquiescence in HM Revenue & Customs' decisions.

> ***[You advise on ways in which acquisitions etc. can be done so as to avoid paying unnecessary tax?]*** *How they can be done to pay the right amount of tax, which is the Revenue's expression ... Yes, and if there is a choice between different ways, and they are equally legal ways, then we will choose the legal way which results in the less of a tax liability than another legal way ... The Revenue have difficulty accepting the tax law doesn't always have the tax maximisation consequences that they would like.'* (Interview 31, infrastructure)

> *Given the ethos of the company and our business, I would say we're relatively low risk. What we want is to do things tax efficiently, but only where we're doing things that are commercial. So the tax follows on from the business side. We don't do things purely for tax avoidance purposes. And we aim to be in the spirit of the law. But that's not to say that we'll just always meekly agree with what the Revenue says. So we're prepared to defend our position robustly and to litigate if necessary.* (Interview 21, infrastructure)

Companies' responses to UK tax authorities, in a more political than civil service sense, could be more equivocal or alienated. Several tax managers expressed the view that the government and treasury show an excessive zeal in pursuit of increasing the tax 'take', to the extent that their pronouncements feel 'anti-business' and insupportable. In particular, respondents expressed resentment at pronouncements that invoked 'moral judgements' in relation to taxation.

> *There's a real drive that HMRC in particular had, about the 'morality' of taxation – 'What's moral, what's the moral thing to do in tax?' ... For a company like this, you can't choose where to pay your tax. You have to pay it where the law says you have to pay it. So if I had my choice, I'd make all the payments in all the territories that we operate in, like Africa, because [it would do the most good there] ... You can't go for this sort of ethical issue ... I think if they'd come and talked to the boards of most multinationals, they'd find people who believe that they were doing absolutely the right thing. If the tax legislation is written in a certain way, then you use all the opportunities provided by that legislation to minimise your bill ... We definitely react quite adversely to the tone that comes out from Government, Treasury and HMRC around how they view large corporates; and some of the statements that are being made make us feel quite uncomfortable about how they view us.* (Interview 32, manufacturer)

> *There used to be sort of clear water between what was evasion (where you'd end up in prison if you did it) and what was avoidance – in which the law is open to interpretation ... But what seems to be happening more recently is 'any type of avoidance is evasion'; and this, I think, becomes counter-productive ... If you want to increase the tax take, increase the tax rate ... rather than messing around with spending so much time and effort which is counter-productive.* (Interview B, infrastructure)

2.6 Obstacles and threats faced by tax managers

Tax managers described a number of difficulties in their work, either current or potentially foreseeable, that were or could be caused by tax rules and rule changes. Foremost among these was the pace of change in, and increasingly complexity of, UK tax rules. Other specific concerns included the need to re-establish the same facts about their operations and structure repetitively year after year.

Respondents reported a range of factors that they felt could or did pose threats to them in carrying out their work effectively: –

- Increasing complexity and a high rate of change in tax rules
  - in particular within the past 4-5 years

- Recent specific changes in certain rules
  - in particular the definition of certain allowances

- The treatment of cross-border transactions, such as
  - handling of inter-company transfers
  - rules over double taxation
  - Controlled Foreign Companies.

- The rate of Corporation Tax not being as competitive as it was.

The high recent rate of change to tax rules was the most commonly-voiced problem, causing extra work and expenditure by adding greater complexity, and making obsolete the expertise born of years of experience: –

> *Constantly changing legislation really, really, really causes us big problems. There are massive amounts of legislation coming out every year. The Finance Act has increased in size phenomenally every single year almost in the last seven or eight years, and everything I learned when I first learned tax is practically obsolete now. I mean, you have to keep on top of your learning. So there is a huge amount of complexity in the industry now. It keeps us all in a job, so that's not such a bad thing; but it does make our lives quite difficult from time to time. (Interview 19, financial services)*

Concern was expressed by some that the UK compared unfavourably with other tax regimes in this respect. One company went as far as to make the following comment: –

> *In terms of the complexity of the tax rules themselves, the tax code, I think the UK has got to a level where it's now even more complicated than the US; and it must be the most complex regime in the world now, certainly of all the regimes that I've seen – both in this job and previous jobs.* (Interview 1, business services)

Some companies were threatened by recent changes in the way certain allowances are defined: –

> *In the last year, there's been a change in the tax treatment of our capital expenditure which is detrimental to us and therefore if it's detrimental, i.e. you pay more tax as a consequence of those changes and so the percentage of tax that we're paying now in our profit is ratcheting up so it has gone up by I'd say £25 to £30 million a year.* (Interview B, infrastructure)

Others mentioned sensitivity to the way taxation on interest paid was handled: –

> *The other area that we're always concerned or interested in is the tax deductions for interest. What we want is to make sure that we get the biggest … where we borrow money, we get full deductibility for tax purposes on interest.* (Interview 30, manufacture)

Concern was also expressed about the impact of the treatment of cross-border transactions, including the rules over double taxation, and the Controlled Foreign Companies rules. Some of these give rise to a 'burden of proof' that tax managers felt to be inappropriate.

> *The UK's international tax policy also has a big impact on the company and the organisation, most noticeably in the controlled foreign company regime, which is another massive admin chore. We have genuine operations abroad. They're not a moneybox sitting in Gibraltar. It's not a British Virgin Islands moneybox company. It's a genuine trading operation.* ***[Presumably once you've proved that, you've proved it?]*** *No, you have to prove it every year.* (Interview 30, manufacturer)

The importance of the competitiveness of the UK tax system was emphasised, and the observation was made that the UK's Corporation Tax rate was no longer so low when compared to other countries as it used to be. In just two cases, it was felt that this was a significant enough issue to impact on the companies' decisions about their activities in the UK:

> *Tax is a cost as far as we're concerned. We're a global business. We look at the global market, the global competitiveness; and tax is not the only factor, but tax is a factor, in terms of where we locate business, where we would make new investments ... Overall we would be looking to reduce the tax burden, but only where the commercial realities allow you to do that. I mean, Kazakhstan may have a zero percent tax rate, but there's no point me going putting my R&D facilities in Kazakhstan if they don't have any infrastructure to do that. Operational factors are always there first, number one, but within that, you do then have a choice ... There are two things here: UK as a base for headquarters of multinationals (and how competitive is the UK in terms of international headquarter location); and the second is UK's competitiveness in terms of the general tax atmosphere (and whether you would make new investments in the UK). And I think currently we would say, well, it's competitive in neither.* ***[Even among its European partners?]*** *Yes, because if you look around – Ireland, it's just sitting out there, and it's got the lowest tax rate and it's got the biggest investment and it's increasing. And now also you're getting a whole load of the new [EU] entrants.* ***[Why are we sitting in this building then, why not elsewhere?]*** *That's the big question now – will we actually be here in a few years' time? That's the debate which is going on. If we think the UK competitiveness is not going to change, then maybe things may change ... The thing is, this is historic. This is where this company grew up. The UK was the headquarters. It's still a UK plc but the fact is that these are now truly global businesses with very little actual commercial markets in the UK. (Interview 29, manufacturer)*

3 Corporation Tax – actual and effective

Tax managers all distinguished between their actual (cash) tax liability from year to year, and the Effective Tax Rate (ETR) that is shown in annual accounts. The former mattered more from the point of view of their ongoing management care, while the latter, as a published indicator, needed to show stability and (for a few) competitiveness over time, to reassure investors.

3.1 Liability to Corporation Tax

The actual size of the current annual CT bill varied considerably across these large groups, from zero to a conventional 30 percent or so of profits.

Their size notwithstanding, several of these groups were presently paying little or no UK Corporation Tax. This was because: –

- They could offset allowances for past losses against current profits, or
- They were making substantial investments for growth, with corresponding allowances against tax, or
- They had negligible profits ascribed to UK trading.

> *A few years back our corporation tax bill would be in the region of approximately about [£5-20 million]. It's gone down drastically because of group losses, especially since we've been taken over. Obviously we've had loans within the group, and the group corporation tax liability has gone down to zero, and we've got losses available for offset.* (Interview 7, retailer)

As they made clear, paying no CT in the UK did not mean less work for them (or their consultants and advisers) – rather, it entailed extensive work to prove the lack of liability: –

> *In the UK we're not paying any CT, because the business is such that we don't have a UK business per se. We still employ people full time to deal with the compliance for a zero tax bill. Because the taxation on dividends alone requires an enormous quantity of man-hours to show that we have little or no taxation on those dividends. Many countries around the world sending dividends to the UK per se are taxable, with credit for the foreign tax. Once you've done the calculation, there's no more tax to pay. You still employ people to do the task. That's compliance. Then add on the accounting people who provide us with information here and overseas. So there are indirect people outside the tax function too, all for a zero sum … plus how many people do you have in HMRC checking our calculations for a zero gain.* (Interview 30, manufacture)

Among the remaining companies, there was considerable diversity in scale and nature of operations, and consequently in actual tax liability.

Nevertheless, all the companies interviewed – including those currently paying zero – reported Effective Tax Rates in a more or less conventional range, between 25 and 32 percent.

3.2 Effective tax rate

Not every group interviewed paid specific attention to their Effective Tax Rate (ETR). Even among those that did, it was unusual to find the company setting a 'target' for ETR. This was partly because the ETR is considerably different from the actual tax that many of these groups were paying, and partly because several of them felt that ETR was beyond their power to influence significantly.

All these tax managers defined ETR as the ratio of tax to taxable profits, as shown in their annual reporting – which of course was very different in several cases from the ratio of actual tax paid to profits.

In the tax managers' view, the importance of ETR lay primarily in satisfying commentators and analysts that the company is capable of delivering sustainable post-tax earnings (as dividends) for its shareholders. So if they had a 'target' in mind for ETR, it was likely to be expressed in terms of stability at or near historic levels, rather than as a quantity to be reduced. Only one tax manager placed ETR at the top of the list of priorities in tax strategy: –

> *The key objective is a stable and sustainable effective tax rate. The second one is probably sound and accurate financial reporting and compliance with the Sarbanes Oxley regime. And then thirdly just acquisition planning, so that we aren't paying unnecessary tax, to the extent that that can be appropriately avoided.* ***[A stable and sustainable effective tax rate is a very specifically defined aim?]*** *Yes. It derives really from our assessment of what's important for shareholder value, and the shareholder places the greatest value on stable and sustainable earnings per share after tax. Our contribution to that is stable, effective tax rate. So we wouldn't be particularly rewarded for having a hugely reduced tax liability one year followed by a greatly increased tax liability the following year. I think the markets and our management must prefer a stable rate which is easy to explain to the market – to the investors.* (Interview 20, business service)

ETR was the subject of a 'target' for some other tax managers, but only in the sense that: –

- It should not be out of line with expectations and within a conventional range (around 30 percent)
- It should not be out of line with 'normal' values found among competitors and similar businesses.

The second stipulation was in effect functionally equivalent to the first, and was part of the broader aim of avoiding 'surprises' and delivering consistency of performance that analysts could observe.

> ***[Are targets set for your effective tax rate?]*** *Yes, I suppose. I mean, the effective tax rate at the end of the day will be whatever the effective tax rate turns out to be. As a general target, my general aim is to have a target of 30 per cent, or as near as 30 as I can get. Having said that, obviously if you've got a fixed level of non-qualified appreciation so you've got a fixed level of permanent businesses, and your retail profit goes down, your effective tax rate must go up.* (Interview 25, retailer)

None of the companies interviewed had adopted a commercial target of driving down its ETR year by year, although several said that their aim was to reduce the actual tax paid.

It was also rare for a company to attempt, with any degree of rigour, to compare its own actual tax liability against that of its competitors, beyond merely checking that they are in a similar ‘range’. The figures required to compare actual tax bills rigorously were not available. Some companies suggested that they were kept informed about this, however, by their advisers (who had greater inside knowledge of other companies).

The tax managers, then, felt that ETR was a quantity that gave external commentators and analysts confidence that a company was being well and consistently managed. That said, it was apparent to some that not all analysts necessarily understood how ETR could be managed by the company to achieve this perception: –

> *One analyst told me he couldn’t understand how I could possibly get it [ETR] anywhere near 30 percent, and I said, ‘Well, if you do good housekeeping which is what we try to do then why not?’ She couldn’t understand it, and she said, ‘Well what do you mean by good housekeeping?’ I said, ‘Good housekeeping is, for example, you go out to the operating companies and say ‘Right, you’ve got an unqualified depreciation. Is it right? Have you reviewed it? When did you last review it against your building portfolio and how many buildings have you got rid of since then? ... And basically taking out all these general provisions (and that’s what’s brought our rate down) is all good housekeeping is – constant challenging.* (Interview 25, retail*)*

4 Tax Departments – structures and activities

The interviews gave insights into the ways different groups define resources, staffing and structures to handle their tax responsibilities (including CT), which are examined here.

4.1 Tax managers themselves

Tax managers in these groups are typically senior individuals with extensive specialised experience in taxation.

Across the groups interviewed, it was unusual for the tax manager to have less than eight to ten years of working experience that related directly to tax as a specialised area of company finance. This experience often included having worked for other (smaller) businesses in a tax-related capacity before reaching their position in a large group.

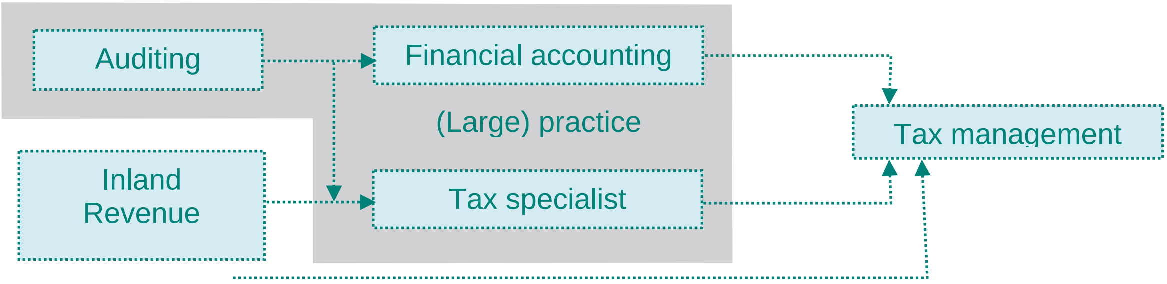
Different respondents held a variety of job-titles, including, among others: –

- Head of Tax
- Head of Tax and Treasury
- Group Tax Manager
- Management Accountant

While their responsibilities in all cases centred on taxation as it affects their company, several (usually, it seemed, in smaller groups, or those with a non-UK parent) included other areas of work within their domain. These other areas included insurances, and roles related to employee pension schemes.

With two exceptions, these tax managers originally gained professional qualifications in accountancy. The exceptions gained their first professional qualification in law. All had typically reached their present positions following one of a range of career paths, as summarised in the diagram below. Most had started within an accountancy practice, and trained there in the conventional ways, normally including extensive auditing work. They then broadened their experience (typically one of the larger) accountancy practices, either in general accounting or migrating to tax as a specialism. From there they moved into ‘client’ organisations of various sizes, and rose to the post they now hold in large groups by promotion and job-changes. Several had started their careers within the Inland Revenue, and then moved outside, either to large practices as tax specialists, and onward toward their present job; or directly into corporate employment.

Figure 2.1 Past career paths among tax managers



Not all had been tax specialists before leaving an accountancy practice and arriving in business.

Irrespective of career details, the managers tended to show a pronounced specialism in their current expertise, which predated their working for their present employers. Several mentioned their participation in the Chartered Institute of Taxation.

4.2 Tax Managers' reporting and roles

Large groups' tax managers have a short line of communication to their board of directors. They have two principal roles: management control and reporting of tax affairs; and strategic input to company plans.

Among these interviews, it was rare to find more than one intermediary, if any, between the tax manager and the group's financial director or equivalent. The exceptions were in groups with an overseas parent, for which the UK is just one market among many.

> *My role reports to the head of the group service centre, who then reports direct into the group Finance Director. The group FD is actually from a tax background himself, so my interaction will be mainly with the group FD in most cases.* (Interview 22, infrastructure)

In the context of the company's management, the tax manager's role is essentially two-fold: –

- Operationally, to ensure compliance, accuracy, and an effective management of the cashflow implications of taxation; and

- Strategically, to guide company decision-making (at board level) by supplying an informed understanding and evaluation of the tax implications of alternative courses of action.

> ***[So you act in two roles?]*** *'Absolutely. That's quite a clear distinction. There is advisory and there is compliance, and obviously the proportion can sometimes be 50:50 but more often than not it's probably 60 per cent compliance with 40 per cent advisory.'* (Interview 19, financial services)

The work for most therefore involves both administrative tasks and a broader expertise-based strategic 'consulting' role.

Administratively, tax managers are responsible for
- the budgets allocated to handling tax (as described in section 4.3, page 34);
- as line managers they are responsible for the control of external agencies (section 4.4, page 37),
- and again, as line managers, for those who work within their 'department' (section 4.6, 40).

Strategically, the expertise vested in the tax manager is obviously important in the group's approach to and formulation of tax policy (whether formally documented or otherwise). This aspect is previously described in section 2.2, page 12.

These large groups, many having extensive overseas operations, adopt a variety of organisational solutions to the deployment of those roles. In particular, where the group includes active trading in many national tax jurisdictions, it was common to find that they devolved local administrative compliance for CT (or its local equivalent) to the countries concerned, or to regional centres: –

> *The tax compliance work for each country is done in the territory where we're located. Wherever we have a company, that company has responsibility to file its tax returns and deal with tax compliance. We have a shared service centre in one country which is doing more of that, and we may migrate more of that activity to that centre, but not the preparation of tax returns because I believe those need tax specialists in their geographic location. My Group Tax team is based in several countries, and does the tax returns for those locations. We do not do, or review, or get involved in the tax return process for any of the other countries, but we do get involved if there are disputes, audits, those kinds of issues – then obviously we will give support.* (Interview 32, manufacturer)

This pattern – local compliance, central control and strategy – seemed particularly to be the 'standard' in businesses such as alcohol and tobacco, where the proliferation of local tax and duty regimes tends to favour maintaining local expertise in compliance.

The logical consequence was that in several interviews in companies with overseas parents, the tax manager in the UK was primarily responsible for the 'administrative' tasks, and played less of a part in the strategic role. There was also a hybrid circumstance, where the tax manager was responsible for a region of the world, both administratively and strategically, while reporting to the global head of tax overseas in the country of incorporation.

4.3 Tax department budgets

It is usually difficult, and often not possible, for tax managers to identify a specific sum that embraces all the costs of administering and handling Corporation Tax in their business.

It was not usually easy for tax managers to identify how much money their company spends in handling CT. The difficulty stems from: –

- The spread of salary costs across several points within the group and the problem of allocating a proportion of each of those to CT, as distinct from the other work undertaken by the same people
- The handling by UK staff of CT or its equivalent overseas as well as in the UK
- The habit in some companies of outsourcing the compliance work to external agents, with CT being just one of several responsibilities that each agency handles
- The extraordinary or one-off costs incurred during mergers, acquisitions or takeovers and paid to external practices, where some but not all of the fees could be considered CT-related
- The reluctance of some companies to discuss how much their management of CT costs them.

As a result, even in tax departments with few employees and comparatively straightforward compliance-only duties (such as were met in the UK offices of some overseas parent groups), it was not always possible to elicit a budget sum or cost that could be attributed to CT alone.

> *It’s not really a budget as such. I have a figure, but some of that covers [fees for] the compliance work, for example, because that person is self-employed. So, say, 50 per cent of my budget covers that person’s ‘staff’ cost. And then outside of that 50 per cent, I have an allocation which I may or may not use. I may go over it. But from one year to another, it’s not specifically allocated.* (Interview C, infrastructure)

Among those cases where the tax manager could offer a view, estimates of the costs directly associated with CT (i.e. the salary costs and external fees, but excluding the actual tax paid) ranged widely: from £25,000 to £2 million per year. Within this very broad range, the level appeared to depend on the simplicity or complexity of the group’s structure, and the extent of its involvement in a multiplicity of markets beside the UK.

So for example a company with operations in the UK alone, and a simple structure, found this an easy question to answer:

> *Our taxation costs are probably about £15,000 to £20,000 a year externally, and a proportion of my time which is small. You could allocate £5,000 of my salary to it for instance. It’s nice and straightforward.* (Interview 15, retail)

On the other hand, a larger global group with activities in many countries and a multi-layered structure found it much more difficult to estimate the global (or even UK) total, whether in terms of budget or spending.

> *We all have budgets, but what the budget is for complying with UK Corporation Tax … I can only hazard a guess. For those very specific purposes of managing the Corporation Tax liabilities, I would say that the budget would be in the order of £2 million per annum.* ***[Roughly what proportion of that is internal and what proportion is external cost?]*** *I would say about 80 per cent is internal, 20 per cent external.* (Interview 13, infrastructure)

Estimates of specific CT-related costs were more precise in companies where there was ongoing spend on outside consultancies that manage compliance, and where expenditure was likely to be roughly the same from year to year.

> *Well if you just say what we almost have to spend with [consultants who also handle compliance] on an annual basis to keep going, we're talking about £300,000 ... Of that 300 I think 50 is really just producing the Corporation Tax returns. You've got about 100 for reclaims, and research and development credits. Then you're probably talking about another 50,000 for other things that need investigation during the year, or questions … And then the balance, about 100 in the last couple of years, is what we've spent on dealing with the enquiries ... Bits of enquiries raised by the Inland Revenue on Corporation Tax returns.* (Interview 3, business services)

Where compliance was handled within the company, any role for consultancies was limited to projects and 'events' (acquisitions etc.), which by their nature were less predictable. Budgeting in those circumstances was necessarily flexible.

> *I have quite a low budget [for external fees] because we don't budget for one-offs, and every year I can tell you that there will be one-offs that we haven't anticipated. But yes, I do have a budget and it hasn't moved much in the last five years. It's about £80,000 as far as Corporation Tax work is concerned. That will be for external advisors. And that may be accountancy advice; it may be legal advice. There's a separate budget for salaries, which I don't really have any control over. It's set at the start of the year and that's what that is ... My overall budget for the department, which would include the salaries and everything else is about £600,000 ... about 90 per cent of which would be about Corporation Tax.* (Interview 6, infrastructure)

It was apparent from several tax managers' accounts of recent company history that spending on the management of CT could vary considerably from year to year within the same organisation, under the influence of events. Structural changes, takeovers or acquisitions, or strategic expansions in the UK or overseas would each impose new spending requirements related to CT, either in planning to minimise CT or its management and administration.

> ***[Do you have a budget for the whole department?]*** *We do, and it's negotiated each year; but it moves because there are things which are unpredictable. So obviously we've got a staffing budget, we've agreed that that's the level of staffing that we've got and then we've got a budget for adviser fees. Say for example when we had the takeover, we needed to restructure. That went through much higher. And the same would go for any situation where we then get an expenditure arising as a result of some change in the company. [****But the adviser's budget, can you tell me roughly how much this involves in a normal year?]*** *I don't actually know. [****Well in round terms, how much does it cost?]*** *Something over £1 million.* (Interview 18, infrastructure)

The major part of this variability from year to year is in external fees rather than internal salary costs – it is the consulting practices that benefit. Salary costs tend to be more stable and predictable, except where a group has taken the decision to relocate or restructure its tax handling personnel, or to outsource tax-related work: –

> *There's an annual budgeting round that the whole group goes through, and I put in what I think the budget ought to be. Sometimes there might be a discussion about it, sometimes there isn't. And then every quarter it's looked at again, so there's a rolling budgeting process. I'd say my budget has remained pretty static but the composition of it has altered. [***In what sort of way?]** *We used to be entirely London based, so shifting people elsewhere has enabled us to buy cheaper people in cheaper space, and so the mix of the salary spend has altered ... [***So you've been able to have more people?]** *Yes, that's how it's turned out.* (Interview 31 - infrastructure)

Otherwise, in more stable times, it seems that tax managers can often take last year's budget as a reasonable guide to this year's need: –

> *The budget is set on the basis of last year's budget, plus or minus adjustments – because if one were to start completely afresh, then no-one would have a clue what the budget actually ought to be.* (Interview 20, business services)

4.4 Allocation of work externally

Most companies interviewed used outsourcing to some extent, to assist with CT work. The pattern of such outsourcing was diverse; with some keeping most routine work indoors, while others look for global outsourcing partners to handle compliance. Some special circumstances – especially mergers, acquisitions, new operations and tax disputes – tended to lead these large groups to consult outside expertise.

Almost every company interviewed gave at least part of its CT-related work to one or more outside suppliers to handle. The portion outsourced could include administrative *or* strategic work. Within this sample there was no consistent pattern discernible that explained the types of work that different groups outsourced, but some indications are given in what follows.

First, some tax managers simply inclined to or avoided outsourcing, based on their own preferences and their interpretation of their own experience.

Second, those that operate in a large number of overseas territories, each with its own tax regime, tended to outsource the compliance work in those territories – especially if their requirements were broader than CT (involving alcohol or tobacco duties, for example). Their rationale for this could include two elements: –

- The degree of local expertise required in each territory, which it would be less economical to host within their own business, either centrally or in each country; and

- The economy of scale and greater consistency that become available if they award this outsourced work to one or a few 'global partners' chosen from among the major accountancy practices.

  Each overseas country has primary responsibility for its own tax affairs. We set the strategy and the direction ... [but] each end market is responsible for its own affairs. (Interview 30, manufacture)

  Although I have responsibility for the tax in [other countries], we effectively outsource all of the compliance in those areas. So I have an overseeing role, I assist with cross-border planning if you like, putting their tax in a group context – because sometimes what makes sense for a local business to do doesn't always make sense from a group perspective. (Interview 6, infrastructure)

  Outside of the [defined, larger] territories and a few of the more complicated countries, it's quite straightforward, because most of our companies are pure sales, marketing and distribution entities. So they really don't have very complicated tax affairs. We're actually moving to outsource most of the markets, so that most of them will use local advisers ... And we're moving to implementing a preferred supplier across the world, to standardise and improve reporting of tax advice. (Interview 32, manufacture)

Third, in territories where a group does little trade or has only a small presence, it may have chosen to outsource rather than over-investing in the local expertise required.

> *We outsource filings in locations where we don't have a significant presence, like continental Europe. We may obtain ad hoc advice on a project basis. Other than that, it's all in-house.* (Interview 2, infrastructure)

Tax managers were more likely to bring in outside help in 'special' circumstances, where the company was involved in a merger or acquisition, setting up a new corporate structure or undergoing a change of structure (whether centrally or in a defined territory).

> *That [budget] does exclude the capital allowances reports, because those are quite complicated projects to undertake. We don't have the resource in-house to do it, and they're quite technical; and a typical report for us, a development project, will cost somewhere in the order of £25,000 for a report. We have had quite a few store openings so there has been £25,000 per report on each of those.* (Interview D, retail)

> *[We use] a variety of international accounting firms and law firms, across a wide range of matters such as analysis of new bits of legislation, advice in relation to various commercial transactions we're undertaking, advice on acquisitions and divestments, whether it's tax, due diligence reviews or whether it's advice on restructuring. All of those. Probably the largest part goes on tax advice on commercial transactions and reorganisations, which the group is undertaking for business reasons, but we want to make sure we don't trip over any tax obstacles ... In our case, almost none of that is on the traditional kind of tax avoidance level. Almost all of it is in support of business transactions which are complex, and on which we need to get definitive tax advice before we can go forward.* (Interview 20, business service)

Disputes with the tax authorities were another occasion for outside help.

> *We've got a dispute with the Revenue at the moment, which looks like it may well go to the Commissioners, and we're spending quite a bit of money on legal advice on that issue. That's for me to pitch to the Finance Director, to say that this is money that we need to spend. And he will either agree on an individual basis or he won't agree. ... This is a multi-million pound item, so the fees are small in relation to the potential gain.* (Interview 6, infrastructure)

> *In terms of advisers, we have some dealings with all of the big four accounting firms. Sometimes when it's a litigation matter, or something to do with, say, a business we've sold and where there's a dispute on tax issues which may or may not come back to us under warranties and indemnities then we may use our main law firm.* (Interview 1, business service)

In summary, then, the decision for or against outsourcing CT-related work stemmed from the interplay of these main factors: –

- Tax managers' personal preferences and experiences,
- The perceived need for specialist knowledge in territories overseas,
- The opportunity for savings by using global partner suppliers,
- Potential over-investment in salaries in territories with small liabilities,
- Special requirements at times of change to corporate structure or legislation, and
- Special requirements to handle disputes with tax authorities.

4.5 Approaches from outside consultancies

External tax specialists called on tax managers, to offer details of tax-saving devices, but managers seemed increasingly to resist these approaches.

Companies are occasionally approached by outside specialists with new initiatives that may alter their tax position.

> *They're coming up with ideas all the time. These big firms, they have bods just working in a room coming up with tax ideas, and they're coming to us and suggesting them, so it's a case of 'Which one do you do?' And they take quite a large cut on that. They might say to you right, we're going to save you £X thousand, we'll have 10 per cent of it or they might say to us 'Right, we want £50K up front.' So whatever happens, you might save some tax or you might not. It's a gamble, if you like.* (Interview E, infrastructure)

> *Well I suppose we'd say we're always open to ideas for reducing our tax bill. We're always on the look out and if we hear of something we'll have a look at it.* (Interview 4, infrastructure)

Several tax managers reported they are resistant to these approaches – often claiming to be more so than in the past – and that the practices have learnt to desist from this activity.

> ***[Do external consultants and advisors approach you with new ways of saving tax?]*** *To a much lesser extent than in the past. And one of the reasons for that is the new disclosure regime, and the new environment on tax schemes – because most of the old schemes don't work any more, and the few that do, or those that do, are probably for a more aggressive company now, rather than a middle of the road company like ours* ***[And the focus, as you said earlier, has shifted away from 'schemes' as such to more structural considerations and being careful about the way in which the company is set up?]*** *Yes. I think this is a permanent change, and I think it's a good thing personally because as an individual income tax payer who feels that they probably pay more than they would like to, I don't see why previously the bolder companies were able to hugely reduce their tax liabilities as a result of wholly artificial arrangements.* (Interview 20, business services)

> *We don't tend to get [those approaches] very much now, because we've managed to train most of them not to. But all of them will say, 'We'll come in and do a big review for you and that review will result in lots of ideas'.* (Interview 32, manufacture)

4.6 Tax department structures

Tax department structures varied widely, depending on the scale and scope of their work, and the extent of outsourcing.

Just as groups varied in the degree to which they outsource their work, whether in compliance or strategic advice, so too did they vary in size. The smallest department interviewed comprised just one person; the largest, over 50.

The numerically smallest tax departments operated in one of two circumstances: –

- The UK subsidiary of an overseas parent, where there was little advisory requirement, and all (CT) compliance work consisted of the collation and transmission of figures to group head office; or

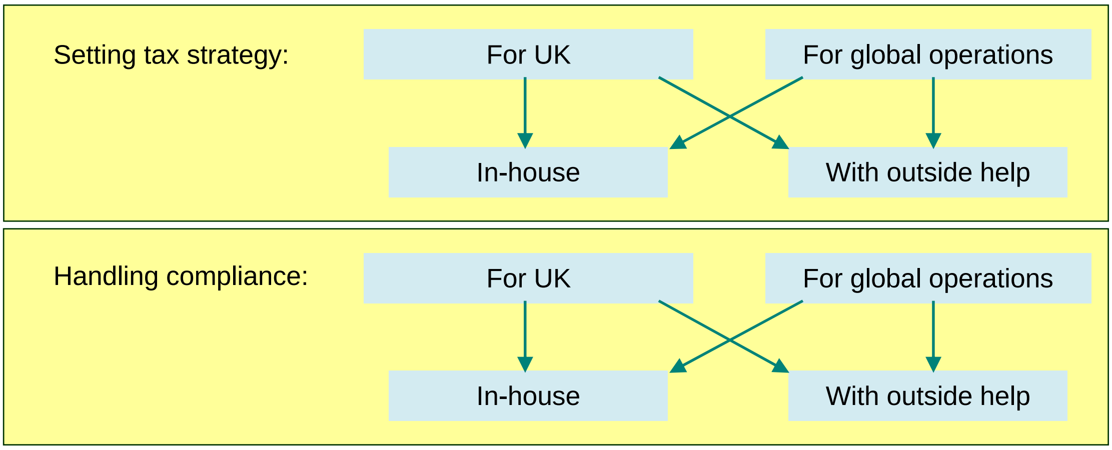
- Businesses where all (CT) compliance work was handled by an external agent, and where any strategic input would be sought from similar external sources.

At the other extreme, companies with widely dispersed activity in many countries tended to have large numbers of tax staff, either grouped centrally or operating in concert from several countries as a 'virtual team':

> *We have a tax department of 55 people in my 4 locations. The way we structure ourselves is as a global team. We have people in each of the locations to focus on the local compliance issues … [People in] the 4 locations do what we call global planning, looking at things like mergers and acquisitions; where should we locate things; if we're going to buy things how should we structure it. ... And then I also have a big group of people who work from the 4 locations and work together as a team doing what we call dealing with risks in different areas ... We have people looking at what I call structural risk, which is all the rules around CFC's, double tax relief, making sure that we comply with all of that, all the requirements under those rules. But we also have people looking at reporting risks, annual reports, Sarbanes Oxley, those kinds of issues. So I've got a planning team, a risk team and ... compliance, I have a very small team that deals with indirect tax, 3 people that deal with VAT and duties.* (Interview 32, manufacture)

Between these extremes in terms of headcount, were businesses that outsourced all local compliance around the world, reserving strategic thinking as a central function; and others that handled both compliance and strategy in-house.

Figure 2.7 – Diversity in tax department roles



The diagram shows how the sample as a whole, despite its small size, manifested every permutation of the ways that a company could organise itself to handle the compliance and strategic functions, in-house or outsourced, for the UK or globally; with the exception that UK-based groups did not outsource their strategic role, entirely, in any of these groups

The tax managers also differed widely in respect of the other tax types that they were involved with. Most were also concerned with at least one of PAYE, VAT, CGT, Stamp

Duty, CCL, land taxes and more (and their equivalents in other jurisdictions). None that were interviewed handled *only* Corporation Tax, although they might have staff working under them who worked on CT exclusively.

As with CT, so with these other taxes, there was considerable variety in the ways different groups structured themselves for compliance and for strategic advice, with options to treat these centrally or at regional or operating company level, and to handle them in-house or through external agencies.

> *We don't do the payroll returns; we don't do the PAYE, all of those kinds of things. But we do give advice to our HR Department on things like pensions, on expatriate taxation structuring, contracts, property and things like that. So we do get involved in an advisory capacity, but we don't do the standard compliance work.* (Interview 19, financial services)

4.7 Incentives applying to tax managers

Tax managers were not apparently in receipt of bonuses or incentives that depended on their performance in cutting tax bills.

These tax managers (and their staff) typically benefited from company performance-based incentive schemes. The basis of such incentives usually included at least one of the following: –

- Overall company performance, based on profit before tax, rather than after
- Performance in compliance, measured by the timeliness and accuracy of forecasts, Returns and payments, rather than in level of tax
- Scorecards of service delivered by the tax department to other 'customer' departments and functions within the group

In no case was a tax manager working under an incentive based on targets for actual tax liability or effective tax rate. Indeed, several could point out why such a basis would be a poor management decision. Achieving reductions in the tax charge featured only as one of a set of objectives.

> *Yes, we have bonuses based on a set of targets. But I think something like the effective tax rate setting at a level would be a silly thing to base a target on, certainly in our business, because it's not very much within my control. If we were to, you could say if we wanted to have a target of reducing the effective tax rate then I could say let's set up business in Jersey or something and close down in the UK. It's not very much in my control therefore it's not a good [measure].* (Interview 1, business services)

> ***[Do you have any kind of bonus incentive based on tax rates?]*** *Not directly, no. I mean, it feeds into how well the company does but we don't have anything that says if you reach tax rate 'X' you get a bonus of 'Y' ... The tax department agrees general targets which are 'balanced portfolio' targets. One of them will be around the numbers, but it is more about being able to manage the forecasting and to deliver timeliness and accuracy. We also have targets in employee satisfaction surveys, how well are the Tax Department operating. We also have targets around, 'customers' is a silly term, but we have customer feedback – how well are we supporting the rest of the business, how responsive are we? Does the rest of the business feel it's getting the advice it needs and the support it needs?* (Interview 2 - infrastructure)

> *Performance targets in this business are always before tax, so the tax number really doesn't have any impact on whether directors get their bonuses or not ... My personal objectives would be to agree another year or something with the Revenue, but no-one else in this organisation would be assessed on tax. It's just not a factor.* (Interview D - infrastructure)

4.8 Tax management systems

Abacus software is in use for Corporation Tax at around half the companies interviewed.

All the tax managers in this study were asked what software or systems they use in-house for CT. The only proprietary name mentioned with any frequency was Abacus. Many of those who mentioned Abacus remarked that it was Deloitte's proprietary system. Otherwise, departments use the reporting 'packs' their outside agency supplies, or manage with a general-purpose spreadsheet application.

Table 2.9 Software used for Corporation Tax

Total:	37
	No.
Abacus	19
Excel	6
Deloitte's (no mention of Abacus)	3
Alpha Tax	3
Tolleys/Tolleys Tax Link	2
Other	8
Don't know	4

5 Working relationship with HM Revenue & Customs

Working relationships with HM Revenue & Customs were generally regarded as effective, and tax managers saw changes in the Large Business Service as potentially beneficial. The interface was still evolving, as Customer Relationship Managers are brought in and start to deliver.

Companies wanted to be seen as candid and open in their dealings with the department, and to foster a good working relationship on that basis.

But several also stated that they would be ready to defend themselves vigorously against challenges from HM Revenue & Customs, if challenged over their interpretation of the rules.

While this subject was not covered in depth with every tax manager, it obviously arose as a topic in many of the interviews, and the key findings are given here.

These tax managers were aware of the organisational changes in HM Revenue & Customs, and in the Large Business Service, that had followed the merger of Revenue with Customs. Several respondents were members of the Large Corporates Forum and other bodies where these changes had been discussed and to an extent shaped.

In general the managers were supportive of the initiatives, especially the introduction of a Customer Relationship Manager (CRM) who could work with them across tax categories as a 'one-stop' contact. On the other hand, they tended to feel the changes were too recent for them to be able to judge whether they were successful. One felt it was disappointing that they still had to deal with separate teams for VAT and CT, and was impatient for a resolution.

> *[**Are there any ways in which you feel that they might improve?]** No, I can't think of any at the moment. If we have a problem with any particular tax issue, it's either [to call the external practice], or just pick up the phone and ask the Inspector directly. I would say they're very, very helpful.* (Interview 7 - retailer)

The most consistent criticism of HM Revenue & Customs from an operational viewpoint – the amount of time and effort that can be required to respond to questions that arise (sometimes repetitively) from the department in response to a company's supplied return.

Answering detailed queries was particularly contentious in the light of a perceived asymmetry – companies felt they were obliged to respond and reply far quicker than HM Revenue & Customs would in turn reply to them.

The managers felt obliged to avoid 'rocking the boat' with HM Revenue & Customs because of the importance they attached to maintaining a good reputation with the authority (as noted in section 2.2.2, page 18). That said, several stated that they were firmly prepared to defend their actions, and their view of what the law allowed, against challenge from the department; and several were actually involved in legal actions against the department at the time of the interviews.

> *As long as it's fair then that's not a problem. What I don't like is when we pay tax, or are asked to pay tax on something that isn't a profit and I'm in dispute with the*

Revenue now over such an item which I'm very unhappy about because it's not avoidance because I can quite understand HMRC being very upset about avoidance schemes. This is just an innocent normal transaction and they're saying, well I don't agree with what they're saying. (Interview B, infrastructure)

6 Conclusions

This exploratory study found a wide spectrum of corporate attitudes and practices in CT, ranging from the ‘aggressive’ to ‘risk averse’. Those are terms which these tax managers were quite comfortable applying to their own policies.

The range of views and practices appeared to result from two main influences. The first of these was differences in corporate styles of management: some companies approach all aspects of their operation in a more risk-averse manner than others. The second was the influence of the tax manager within that management style. Some of these tax managers, as individuals, were more adventurous than others.

These respondents, irrespective of their place in this ‘spectrum’, reported that they believed that increasing burdens have been placed on the tax management function in recent years. They said that tax rules have been changing faster than in the past, with greater complexity within the rules at any one time. This, together with the 2004 rules on disclosure of schemes, and the publicised outcomes of some legal challenges, reportedly discouraged at least some organisations from tax planning activities that they might have considered in the past.

The discouragement was apparently greater in the world of *operational* than in *structural* tax avoidance: several of these companies saw much reduced scope for reducing taxation in relation to their everyday trading, but remained actively interested in structural solutions (to incorporation, acquisitions, start-up and business locations) that could reduce their liability to CT.

On the other hand, some respondents stated that greater complexity, allied to a CT rate that is higher than in several other European countries, might be a deterrent to placing future investment in the UK. Two of the 37 companies interviewed believed that they might choose to relocate their headquarters overseas in the future, for tax reasons, so long as all other operational needs could be met in the destination country. Both of them were multinationals with UK origins, and among the largest interviewed.

Finally, there is a hypothesis that might be inferred from this set of companies: that more aggressive practices are more likely to be found in companies with fewer shareholders, and perhaps especially where major shareholders are part of the management. But the basis for this speculation is only three of the 37 companies interviewed in this sample, so it would need to be tested across a much broader sample before being accepted. The degree to which tax managers are prepared to be entirely candid in research interviews may preclude such verification.

Appendix A
Technical report

The following pages give details of the procedures and stages that FDS followed in securing the 37 interviews described in this report. Descriptions are given of: –

- The sampling process
- Opt outs and refusals
- The advisory mail out
- The procedure for making appointments
- The interviews themselves
- The feasibility study
- Interviewing dates
- The analysis of findings
- The need for anonymity
- The achieved sample profile

Sampling process

The agreed target was to achieve 35 completed interviews, in two stages – an initial feasibility test, comprising five interviews; and a later 'main stage' with a further 30 interviews. In the event, 32 interviews were completed in the main stage, yielding a total of 37.

In preparation for the sampling, HM Revenue & Customs supplied to FDS a listing of 314 businesses that fall within the scope of its Large Business Service (LBS).

For the feasibility stage this list contained no contact details for the individual responsible for CT. A random sample of 50 businesses was drawn from this list and FDS telephone interviewers contacted those companies to fill in missing names by conversations with switchboards, personal assistants and colleagues. At this point an interview was not sought; the intention was solely find out their name, telephone number, and correct contact address (including email address if available).

In the event full contact details of 34 individuals in different businesses were identified and used for the feasibility stage.

For the main stage HM Revenue & Customs attempted to populate the list of 314 businesses by appending details of the LBS Customer Relationships Managers CT contacts. However, this list was not complete, and again FDS telephone interviewers sought to fully populate those fields before the sample was drawn.

After extensive searching, details of 243 contacts within this business list were identified.

HM Revenue & Customs has a policy of trying to keep to a minimum all contact with major businesses about research. As a result it was decided to use sample sparingly, and ensure that as few businesses were contacted as possible. Therefore, 75 businesses were drawn for use in the first round of the main stage; and once this was exhausted a further 40 businesses were drawn to complete the survey and achieve the target number of interviews.

In practice, across the study as a whole (including its feasibility stage) the notification letter was sent to a total of 148 people. It resulted in 45 refusals to take part. Among the remaining 103 available candidates, many were unable to commit to an appointment (because of annual leave or other commercial pressures). Nevertheless not all the available candidates needed to be contacted in order to secure the 37 interviews that are reported here.

The table below breaks down the sample of businesses supplied and used for the feasibility study, in chronological order:-

	Number
Businesses supplied by HM Revenue & Customs	314
Sample drawn for usage	50
Name and full contact details of individual responsible for CT	34
Letters sent to candidate interviewees	34
Interviews achieved	5
Consultant interviewer unable to contact 'no reply'	9
Refused to be interviewed	8
Incorrect addressee	1
Letter not received and therefore refusal	1
Unable to take part within survey time frame	1
Not contacted as target interviews achieved	9

The table below breaks down the sample of businesses supplied and used for the main stage, in chronological order:-

	Number
Businesses supplied by HM REVENUE & CUSTOMS	314
Businesses with full contact details of individuals responsible for CT identified	243
Sample drawn for advisory mail out 1	75
Letters sent to candidate interviewees	75
Interviews achieved	19
Consultant interviewer unable to contact named individual 'no reply'	28
Refused to be interviewed	28
Sample drawn for advisory mail out 2	40
Interviews achieved	13
Consultant interviewer unable to contact named individual 'no reply'	13
Refused to be interviewed	9
Not contacted as target interviews achieved	5

Opt outs and refusals

All but two of the candidate interviewees that opted out of the survey cited commercial pressures or annual leave as their reason for not participating. The other two queried the purpose of the research and claimed not to see any value in taking part.

Advisory mail out

All individuals selected to take part were sent a letter advising them that the survey was taking place. The letter (which can be found in Appendix B) asked for cooperation and specified the objectives of the study. It also provided contact details of the project manager at FDS, should the individual wish to opt out.

Making appointments

Members of the interviewing team approached candidates to seek appointments. The initial approach was either by telephone or email. The major reason for non-conversion at this stage was non-availability – candidates being away from their offices at the required period (on holiday, for example) – rather than being unwilling to take part.

The interviewers then made appointments and visited respondents at their place of work for interviews lasting between 60 and 90 minutes.

The interviews themselves

The interviews were necessarily exploratory in nature, but structured using a topic guide (shown in Appendix C). The topic guide covered three main subject areas: –

- The individual and the department
  - how the group structures itself (and funds itself) to handle its CT responsibilities

- The focus in tax management
  - the priorities and pressures that determine tax practice within the group

- The work
  - how the manager and department performs or allocates its functions
  - including consideration of its working relationship with HM Revenue & Customs

All interviews were tape-recorded, and full transcripts were produced for analysis.

Feasibility study

At the outset of the study, an initial five interviews took place, to test: –

- The procedures for recruitment
  - including the reliability of the approach to identifying candidates,
- The willingness of tax managers to take part
  - and to co-operate within the interview itself, and
- The interview content (the topic guide)
  - for completeness, suitability and relevance

This feasibility stage yielded two main methodological findings.

First, the study approach was workable – tax managers were willing to take part, and there did not appear to be any substantial skew in the ‘refusals’ in terms of company size, place of incorporation or type of business. The senior level (qualitative consultant) approach to candidates was very successful in securing interviews, with a high conversion from initial contact to completed interview. The tax managers interviewed were willing to open up and talk relatively freely about CT planning (reticence to talk even at the level of the principles had been a concern before embarking on the programme). The topic guide also worked well, to accommodate groups with very different sizes, operations, structures and policies.

Second, even within just five interviews, a broad spread in attitudes and practices emerged, ranging from highly risk-averse (those reluctant to contemplate any ‘devices’ for tax planning) to others with an ambitious programme of tax-saving activity.

After presentation and discussion of the findings from those pilot interviews, and our recommendations for taking the study forward, it was agreed that: -

- As broad a spread of industrial and commercial business types as possible (within the ‘large groups’ definition) would be delivered, to ensure balance and coverage,

- The identities of companies interviewed would continue to be disguised, to protect commercial confidentiality and ensure the anonymity of participants.

One consequence of this is that when describing ‘who said what’ in this report, extremely broad sector definitions have been used, as described in section 1.4 on page 10.

The feasibility study also indicated that an extended fieldwork period would be needed to ensure the availability of interviewees – particularly through the summer months.

Interviewing dates

The five pilot or feasibility interviews took place between 10 and 20 January 2006. The subsequent 32 'main stage' interviews happened between 13 July and 6 September 2006.

Analysis of findings

First, the interviewers prepared summary 'keynote' documents to accompany the transcript from each interview. These were then reviewed by the leader of the qualitative team, and discussed as necessary with each interviewer.

The next step was to review each transcript in detail using a systematic process of sifting, summarising and sorting the material according to key issues and themes. The subjects and strands that emerged in this content analysis are the beginnings of a thematic framework.

The analysis then proceeded by collating and re-ordering the transcript data, according to this thematic framework. FDS summarized the data from each interview transcript under the appropriate thematic heading of the thematic matrix – and allowed the thematic structure to expand or evolve as necessary in this process. The result has been to exemplify, qualify and define explanations and patterns, and to show how views and practices differed across the sample.

The evolved thematic framework was then used to shape a presentation and this report.

The need for anonymity

To ensure an open and frank exchange of ideas and information between respondents and researchers, confidentiality and anonymity was a key component of this project. This had several consequences for this report: –

- Figures (for example, a company's turnover or profit) are reported in deliberately broad bands;

- Businesses are referred to using five broad 'super-sectors':
    - Infrastructure (inc. construction, transport, energy)
    - Manufacture
    - Business services
    - Financial services
    - Retail

Direct quotations from the interview transcripts have in some examples been altered slightly, to maintain anonymity. In most cases quotations are attributed to a specific interview numbered according to the scheme shown in the following section.

Achieved sample profile

The adjacent table shows the characteristics of the 37 interviews achieved, in terms of five broad ‘sector’ definitions and place of incorporation.

It will be seen that the largest representation is in what is labelled the ‘infrastructure’ category. But the definition adopted here was deliberately broad (in order to disguise the identities of several more-or-less unique enterprises). In practice the infrastructure group itself is composed of a very broad range of business types.

The importance of the UK versus overseas as source of turnover or profit varied greatly between companies, with UK revenues ranging from one hundred to as little as three percent.

Global business size (as measured by turnover) also varied considerably, from annual revenues of millions to billions of pounds.

Table A.2 Sample characteristics

		Business sector					Place of (parent) incorporation	
Interview number ...		Infrastructure	Manufacture	Business services	Financial services	Retail	UK	Not UK
Pilot stage	A			•			•	
	B	•						•
	C	•					•	
	D					•	•	
	E	•					•	
Main stage	1			•			•	
	2	•					•	
	3			•			•	
	4	•						•
	5		•					•
	6	•					•	
	7					•	•	
	8				•		•	
	9				•		•	
	10				•			•
	11				•		•	
	12				•		•	
	13	•						•
	14					•	•	
	15					•	•	
	16					•	•	
	17			•			•	
	18	•						•
	19				•			•
	20			•				•
	21	•					•	
	22	•					•	
	23				•		•	
	24		•					•
	25					•	•	
	26				•			•
	27			•			•	
	28	•						•
	29		•				•	
	30		•				•	
	31	•					•	
	32		•				•	
Counts		**12**	**5**	**6**	**8**	**6**	**26**	**11**

Appendix B
Notification letter

The following is the text of a letter that was mailed to all candidates for interview before any recruitment began.

Dear [name]

Tax Department Research

I am writing to ask for your assistance. HM Revenue & Customs is currently conducting research into the way large groups manage their tax liabilities. In relation to Corporation Tax we are specifically keen to gain a greater understanding of groups':-

- internal structure – to contextualise tax departments
- organisation dynamics – influences that bear upon and goals set for tax departments
- attitude, assessment and contingencies for risk
- wider group objectives
- relationships with tax authorities
- tax planning strategies employed.

To achieve this we have commissioned FDS International, an independent market research agency, to undertake research on our behalf.

From 3rd August you may be contacted by an FDS consultant who will arrange an interview with you. These will be conducted face-to-face, last approximately 90 minutes and will take place at a time and location convenient to you. The information you provide will be used solely for research purposes and will be treated in strict confidence in accordance with the Data Protection Act. In compliance with the Market Research Society code of conduct, FDS will only report back to HMRC general findings, which will in no way identify individual people or companies.

If you do not wish to take part in this research or be contacted in relation to this survey, please contact William Ullstein, Project Manager at FDS *[email address and direct telephone number]* by 3rd August. In order to preserve your anonymity please quote your reference number *[unique ref. no.].*

If you wish to confirm that this is a genuine HMRC research study then please call me on **020 7147 2881**. There is no need to identify yourself or your company in doing so (please quote your reference number).

We believe you are the most appropriate person to speak to. However, if you consider another person in your organisation is better placed to answer questions on the proposed topics, we would be grateful if you can pass their contact details to William at FDS.

We appreciate that your organisation may have been asked to participate in some other HMRC research recently. However, we value your input and would still like to talk to you.

Yours sincerely

Francesca Lemetti

Research Officer

Appendix C
Topic guide

HM REVENUE & CUSTOMS LARGE GROUPS DISCUSSION GUIDE – MAIN STAGE

NOTES TO INTERVIEWERS

We are exploring how large groups behave with respect to Corporation Tax (CT). The same people or departments may also deal with other taxes, including VAT, Income Tax and Excise duties. They may also have direct or indirect responsibility for taxes under other (non-UK) regimes. We are not interested directly in these others, except where there are interesting contrasts or parallels between the group's handling of CT and any of them.

The interview structure assumes you will have briefed yourself on the Group, its background, size, status and international connections using publicly available sources, including the published Report and Accounts.

Remember that if the group has a foreign parent, UK CT may be a minor part of larger *group* accounting, more a case of planning the timing and jurisdiction in which tax is paid i.e. the goal is to assist in the minimisation of overall *group* tax. The overseas territory will probably give double tax relief for UK tax incurred up to the maximum of that territory's tax.

Where respondents are asked about *costs* in this interview, we are not concerned with *exact* measures, but want to gain an estimation of the size of the sums concerned, of how they are apportioned to tasks, and by whom.

INTRODUCTION

Recap purpose of FDS research – to aid HMRC knowledge and understanding by providing a more complete picture of large groups' practices with respect to CT. The respondent's participation and input will contribute to an anonymised report that will illustrate the variety of circumstances and approaches to CT among large groups, spanning a range of commercial categories and types of organisation. We will show contrasts and similarities in views and practices across all the companies that we interview.

Remind respondent that the interview will be strictly unattributable – neither the individual nor the group will be identifiable in our reporting.

THE INDIVIDUAL AND THE DEPARTMENT

- Establish brief details of interviewee, including age, qualifications, career history, and confirm their role e.g. are they global or local tax director.

- Recap nature of the Group and its operations that are relevant to CT (size, outline history where relevant, geographic and commercial spread of operations).

- Does the Group have a foreign parent? If so, where is the parent based?

- Does the Group have significant overseas investments? If so, what is the approximate split of revenue/profit between the UK and overseas territories?

- Confirm company status e.g. plc.

- Ascertain how the Group is structured to manage CT
  - the department involved
  - its other roles
  - number of people, organisational structure, lines of reporting (an organogram)
  - the age and career history of other main people involved
  - information inputs to the department that form the basis for CT accounting
  - where and by whom are the key decisions taken about tax affairs – for the UK; for overseas reporting
  - third parties involved; and in what capacity.

- How has the size of the tax bill (CT) - UK and non UK if relevant - that the department is responsible for varied over recent years, and reasons for significant fluctuations.

- What other taxes (UK and other authorities) does this department administer and how significant are they relative to UK CT, in terms of absolute amount and resource dedicated to managing them

Checklist for consistency between interviews *(some of the following may be accessible from the group's annual report, and so could be filled in before the interview)*:
All of the following will be disguised (set into broad banded categories) before any reporting

Size of group – annual turnover	
Size of group – total employees	
Place of incorporation/ownership (UK, USA, elsewhere)	
Proportion (%) of total group profits attributable to UK operations	

- What is the department's budget to fulfil its duties and role *(if tax manager unaware skip this section)*
  - how is this set, and by whom
  - how does it alter; has it changed over recent years
    - what flexibility is available within the budget, and why
  - what factors have led to it changing, and why
  - what is the administrative cost for dealing with CT ...
    - internal costs
    - external costs – payments or fees for external help
    - have internal/external costs increased over the past year
  - how do these costs break down by type – for example compliance; structural tax advice; strategic tax-related planning; auditing internal work; disclosure or transparency requirements; inquiries; litigation
    - to whom do external fees go; for what tasks
    - how does the group choose external firms
    - how does the company evaluate the effectiveness of such external spending.

Checklist for consistency between interviews:
All of the following will be disguised (set into broad banded categories) before any reporting

Annual budget or cost for dealing with CT	
(a) internal (*i.e.* salaries)	
(b) external (*i.e.* consultants, advisers, intermediaries)	

- What IT systems does the department operate that are involved in CT administration

- Control of the department
  - who does it report to, and how
  - where does the tax function sit within the group.

- What are the priorities and objectives set for the department in CT matters.

- We are interested in the differing extents to which companies pay attention to managing their *Effective Tax Rate*, either from year to year, or in comparisons against other businesses. How much importance does your business attach to the effective tax rate

- How are effective tax rates calculated.
  - on a UK-only, or worldwide basis
  - how are deferred sums, brought forward sums or reserves handled in the calculation

- (Multinationals only) How are effective tax rates viewed in your company's broader international or global perspective.
  - how does the UK position compare with other areas of operation
  - do tax/CT considerations affect the company's view of the UK as a place to do business (if so, how)

- Are targets set for effective tax rates; if so
  - by whom
  - on what basis (for example, by comparison with history, or other companies, or other jurisdictions)
  - with what aim (whose attention to effective tax rate is being catered for)
  - how successfully are those targets met
  - what incentives and bonuses, if any, are contingent on meeting those targets *(ask for examples).*

- What other targets apply to the department as a whole, and/or to tax managers
  - who sets these
  - how are they measured and monitored, and by whom
  - how do they change over time – are there progressive goals from year to year.

- How is the requirement to meet priorities and targets reflected in remuneration and other incentives, for tax managers or other financial officers.

- What constraints and restrictions inhibit the department in meeting its objectives
  - what are their most difficult challenges – keeping up with complex legislation, recruiting skilled staff etc.

- To whom is the department responsible in CT affairs
  - what are the roles of and constraints imposed by ...
    - the Board, management (group and constituent businesses),
    - shareholders,
    - auditors
    - Governments, tax authorities and other regulators
    - the broader 'public', UK and overseas.

- How do the department's responsibilities to these influences shape its activities
  - do they create burdens or opportunities
  - is the department a cost-centre or profit-centre in its own right
  - how does this influence what it does and the way it works.

THE FOCUS

- What does tax management contribute to overall assessments of how well the group is doing
  - in its own assessments
  - in the views of shareholders, investors and commentators.

- Are divisions or constituent companies measured on pre-tax or post-tax results
  - how does this distinction affect the group's tax strategy and practices.

(Take care on use of language ['conservative', 'aggressive'] when talking about adopted strategy)

- How does the group balance *minimising tax cost* versus *minimising tax risk*
  - how would the group characterise itself in its approach to tax affairs [maybe probe conservative or aggressive if they don't volunteer this]
    - how does this preferred position manifest itself (in what way does this stance show itself)
    - what rationale underpins the position adopted (e.g. certainty versus opportunism)
  - has this changed in the recent past
    - if so, under what influences
  - is this expected to change in the near future
    - if so, under what influences
  - what part, if any, do HMRC's penalties for submitting late or incorrect returns play in this risk assessment.

- Do different stakeholders adopt different stances on the 'risk' position – the department itself; the group's management; professional advisers; analysts, investors, shareholders
  - who pulls in which direction in this context
  - who prevails, and why
  - what compromises are reached
  - how content is each party with the adopted position.

- What tools are available to the group to help it minimise its tax exposure
  - structural solutions
  - tax planning activities
  - where do those 'tools' originate from
    - external advice and consultancy
    - internal innovation and creativity
  - does the company maintain an active search for ways to minimise its tax exposure
    - if so, how, and through what channels; is there an ongoing 'budget' or retainer for this.

- What is the company's approach to provisioning for CT liabilities
  - how do you deal with uncertainty over the eventual amount of CT you will have to pay
  - and what is the practice

- How do you deal with quarterly payments
  - how are they managed
  - how are they estimated

- How easy would it be, or has it been, for the group to reduce its tax bill, through
  - structural re-engineering
  - adoption of tax management tactics and schemes.

- What drives, and what inhibits, initiatives in these areas
  - what external and internal sources and pressures
  - has the group changed its receptivity to such initiatives (in either direction)

- For companies with a US parent or US listing, what effects has Sarbanes Oxley (SOX) had on decisions the company makes and for non-US listed companies, have they nevertheless felt the impact of SOX
  - what pressures from outside the UK impact on their decisions.

- From time to time the government changes the CT rules in various ways. Would the group be more sensitive about changes in some areas more than others
  - which are the types of change that would give the group more cause for concern
  - for example:
    - an increase in the basic rate;
    - changes in the ways certain allowances are treated (which allowances?)
    - changes that affect your company more than your competitors
      - what possible changes could have such an effect
      - a more severe level of penalty for returns that were 'unreasonable' or 'deliberately understated'
  - what are the likely responses that the group would make to such changes
  - if changes prevented existing tax planning, would the company simply search for new alternatives to adopt?
  - what difference, if any, would it make if the tax on which penalties is calculated was *before* group relief and losses (i.e. unlike now, penalties could not be avoided by offsetting group relief or losses against culpable tax?)

- Several companies have noted concern around a perceived hardening of the government's position on tax planning methods that affect CT
  - do you agree that this has become more difficult
  - what has been the influence of that trend on the way your company handles CT
    - has it eliminated CT planning
    - has it led to a search for new solutions with the same objective

- What are the likely responses that the group would make to ...
  - greater prohibition or regulation of schemes and tax management processes already in place
  - a noticeable increase or reduction in a competitor's effective tax rate.

THE WORK

- Has the group undertaken any planning that they are obliged to declare since August 2004 under avoidance scheme disclosure legislations
  - if so, which and where
  - what is the impact of this on tax liability and the effective tax rate
  - from where did the impetus come to adopt this planning
  - how and by whom was it initiated and authorised
  - how is its contribution or effectiveness evaluated.

- Has the group implemented/operated any other specific tax-planning
  - if so, which and where
  - what is the impact of this on tax liability and the effective tax rate
  - from where did the impetus come to adopt a scheme
  - how and by whom was it initiated and authorised
  - how is its contribution or effectiveness evaluated.

- If no schemes used, any particular reasons why they do not use them.

- What sources of information or inspiration are available and used for advice that would minimise tax liability, in the UK or elsewhere.

- Where do these sources communicate with the organisation
  - at what level, how often, in what form.

- What processes of review, scrutiny or evaluation do tax planning initiatives and proposals receive.

Internally Or Externally

- What influences the company in deciding for and against developing and adopting such ideas
  - what are the key drivers, upside and downside
  - what are the respective roles of certainty and predictability; opportunity and gain.

Attitude/relationship with HMRC

- How does the group relate to HMRC
  - at what level in HMRC is your primary contact
    - Large Business Service - case director or Client Relationship Manager
    - other
  - do you or your company have other informal links into HMRC or the Treasury
  - do you participate in consultations (formally or informally) or in any consultative forums?

- How would they characterise the relationship; for example ...
    - open and full disclosure, versus guarded or minimalist
    - 'compliant' versus 'aggressive'
  - how is this different from the position in other countries.

- What relationship with HMRC does the group want to have?
  - how would they characterise the 'ideal' working relationship
  - what steps (by themselves or HMRC) would help to achieve this ideal.

SUM UP AND CLOSE

- Are they willing to be re-contacted in the future to clarify any points made?