

TAXREP 67/05

PARTNERSHIP ENHANCEMENT PROGRAMME

TAX ON THE BOARDROOM AGENDA

Memorandum submitted in December 2005 by the Tax Faculty of the Institute of Chartered Accountants in England and Wales to the HM Revenue & Customs in response to a letter dated 7 November 2005

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WHO WE ARE

1. The Tax Faculty is the focus for taxation within the Institute of Chartered Accountants in England & Wales (ICAEW), a Professional Body representing some 127,000 members with a Royal Charter obligation to act in the public interest. The Faculty is a centre for excellence and an authoritative voice for the Institute on taxation matters.
2. We work in the public interest to promote enterprise, innovation and sustainable growth in a socially responsible business environment. Our strength and knowledge is drawn from that of our members who hold the world's most highly respected finance qualification. They work in every sector of the economy, size of business and public body, from FTSE 100 boardrooms and government departments, to high street practitioners, small businesses and charities.

GENERAL COMMENTS

3. We welcome the desire of HMRC for greater engagement and discussion with businesses and other stakeholders. The questionnaire is an interesting and useful development and we look forward to seeing the results.
4. It is important that this initiative is positioned correctly. We believe that this programme will obtain the maximum benefit if it is designed to increase understanding of the issues and, where appropriate, raise standards, to the benefit of all stakeholders. Most companies will wish to work within best practice corporate governance procedures, but they may resent what could be interpreted as interference in how they run their business and the ability to undertake tax planning that is within the law.
5. We believe that there is a growing lack of trust between the various stakeholders in the UK tax system. This was highlighted Loughlin Hickey, Global Managing Partner for Tax at KPMG, at our annual Hardman Lecture in November 2005. Both sides need to understand and appreciate the concerns faced by the other side and we are anxious to assist in this process. We recommended in our 2005 Pre Budget Report submission that a new joint forum should be established to consider business tax policy. One of its key objectives should be to rebuild trust and confidence in the UK tax system for all stakeholders. We are committed to working closely with all of those who have a stake in the UK tax system to address this issue in an open, constructive and transparent way.
6. Given that most of the questions are posed specifically in relation to tax as a boardroom issue, we have not completed the questionnaire. Instead, we have set out below what is expected of a chartered accountant engaged in business (whether as a director or not) and then set out some comments on the relevant questions.

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PROFESSIONAL CONDUCT EXPECTED OF A CHARTERED ACCOUNTANT IN BUSINESS

The public interest

7. A distinguishing mark of a profession as distinct from, say, a trade association, is its public interest role. The accountancy profession's public consists of clients, providers of credit, governments, employers, employees, investors, the business and financial community, and others who rely on the objectivity and integrity of professional accountants to contribute towards the orderly function of commerce. This reliance imposes a public interest responsibility on the accountancy profession. The public interest requires the reporting to the ICAEW's professional conduct team of acts of misconduct which could adversely affect the good name of the profession.
8. Although many of our members are in practice, the majority of our members are in business and many boards of directors will include chartered accountants. Our professional rules and principles apply to all of our members, whether in practice or business, although there are specific conduct rules for each of these areas.

Liability of members to disciplinary action

9. The ICAEW's disciplinary bye-laws state that a member is liable to disciplinary action in a number of circumstances: Whilst many of these relate to professional practice, the key ones are relevant to all members, as follows:
 - if in the course of carrying out professional work or otherwise he has committed any act or default likely to bring discredit on himself, the Institute or the profession of accountancy; and
 - if he has performed his professional work or the duties of his employment, or conducted his practice, inefficiently or incompetently to such an extent, or on such a number of occasions, as to bring discredit on himself, the Institute or the profession of accountancy.

Professional ethics

10. Section 1.2 of the Handbook sets out our guide to professional ethics. This also includes specific guidance for members in business (the latter being expanded with additional guidance added in 2004). The guide to ethics sets out five fundamental principles that chartered accountants are expected to observe, as follows:

Integrity

11. A member should behave with integrity in all professional and business relationships. Integrity implies not merely honesty but fair dealing and truthfulness. A member's advice and work must be uncorrupted by self-interest and not be influenced by the interests of other parties.

Objectivity

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12. A member should strive for objectivity in all professional and business judgements. Objectivity is the state of mind which has regard to all considerations relevant to the task in hand but no other.

Competence

13. A member should undertake professional work only where he has the necessary competence required to carry out that work, supplemented where necessary by appropriate assistance or consultation.

Performance

14. A member should carry out his professional work with due skill, care, diligence and expedition and with proper regard for the technical and professional standards expected of him as a member.

Courtesy

15. A member should conduct himself with courtesy and consideration towards all with whom he comes into contact during the course of performing his work.
16. Section 1.4 of the Members' Handbook sets out specific guidance for members in business. This covers financial and accounting responsibilities together with conduct in relation to defaults and unlawful acts by or on behalf of a member's employer.

The duty to report

17. Where it is in the public interest to do so, members should report to the ICAEW any facts or matters indicating that a member and/or firm may have become liable to disciplinary action. In determining whether it is in the public interest to report such facts, the ICAEW Council guidance is to report any:
- offence involving dishonesty, fraud or cheating;
 - imprisonable offence under the Company Securities (Insider Dealing) Act 1985, the Insolvency Act 1986, the Company Directors Disqualification Act 1986, the Financial Services Act 1986, the Companies Acts 1985 and 1989, the Financial Services and Markets Act 2000 or any comparable piece of legislation in the corporate or financial services spheres; or
 - offence for which he has received a custodial sentence, whether suspended or not.
18. More generally, Council has also indicated that it is in the public interest that a member's conduct should be considered where a member has or may have:
- performed his professional work or the duties of his employment in a grossly incompetent manner;
 - committed a serious breach of faith in a professional respect; or
 - committed a serious financial irregularity.

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COMMENTS ON THE QUESTIONNAIRE

19. We set out below our responses to the relevant questions.

Question 3 Do you think a dialogue with HMRC at Board level would be useful in any of the following areas?

20. We think a dialogue would be useful in all of the areas identified. We see no reason why HMRC should not share its views on tax risk with corporate taxpayers and, conversely, that companies should not share how they manage tax risk. We believe that this would help both sides to identify common risk areas. HMRC also need to understand that any risk analysis also needs to consider the burdens of compliance costs.
21. As mentioned in the General Comments section, in our representation on the Pre Budget Report, we suggested that a new tax forum be established.

Question 4 What impediments (if any) are there to having a constructive dialogue with HMRC?

22. We stated in our 2005 Pre Budget Report submission that there is a lack of trust between taxpayers and those who administer the tax system. We believe that there a number of reasons for this, but trust is a fundamental part of the UK tax system which once lost will not be regained easily. Both sides need to understand and appreciate the concerns each other face and this requires constructive dialogue and transparency, a willingness to listen, and the ability to face up to and address problems.
23. The corporation tax and VAT systems have accrued considerable complexity and uncertainty. We believe that uncertainty is undermining the ability of business and Government to plan and make investment decisions, as well as increasing the unpredictability of tax receipts. A series of recent and upcoming judgments at the European Court of Justice are likely to increase uncertainty. These include not only the recent case brought by Marks and Spencer but the forthcoming case concerning the UK CFC rules and rulings related to partial exemptions of VAT and the VAT carousel rules.
24. The new tax avoidance disclosure regime has now bedded down and, we think, generally been successful in discouraging taxpayers from using artificial tax avoidance schemes. However, the resulting announcement of responsive measures, often with key details still to be developed, has further increased the uncertainty and complexity of the tax system, and sometimes may lead to further opportunities for avoidance. From our members' experience, we think that this increasing uncertainty is affecting businesses' decisions over whether to invest in the UK. We are concerned that much of the current anti avoidance legislation will ultimately be counter productive, as reduced businesses investment in the UK leads to lower tax revenues than would otherwise have been the case.
25. The longer term answer to these issues must centre on the need for a simple corporate tax system and reasonably competitive tax rates. Against a background of ever increasing globalisation and a likely push for simplification from our European competitors, we are

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concerned as to whether our corporate taxation system is robust enough to face these challenges and whether it needs more radical reform to ensure that the UK remains internationally competitive. We think that the new joint consultative forum should also undertake a strategic review of the UK corporate tax and VAT systems.

Question 5 Please rank the 3 most important direct and indirect tax matters facing your Board?

26. We are concerned that UK tax rates and policies are becoming uncompetitive as compared to those of other countries. One of our ten tenets is that the UK tax system must be competitive. The main UK rate of corporation tax was once competitive but many other countries now have a lower rate, not least the 12 ½% rate in Ireland. The UK also has a cumbersome and highly complicated system for giving double tax relief, whereas most other European countries operate an exemption system. The compliance costs of our system are considerable and we are not convinced that the amount of revenue justifies the retention of such a system. We believe that the UK needs to have an informed debate on the competitiveness of its business tax system.
27. Tax compliance costs will vary according to the size of the business but previous studies have already shown that they fall disproportionately on smaller businesses. Whilst we appreciate that there are a number of initiatives to measure and also reduce the burden of compliance costs, we believe that it is essential that there is a clear commitment by government to reducing compliance costs.

Question 6 Do you expect the importance of these issues to change over the next two years?

28. To an extent, the relative importance of these issues will depend on any further changes to the tax system. With global competition increasing, we think that the UK's competitive position on tax will come under increasing scrutiny, not only in respect of the headline rates of tax but the wider question of compliance costs and the overall business environment.

Question 7 In what areas of your business is tax risk management important?

29. As a professional body at the vanguard of encouraging and upholding high standards of governance and standards generally, our key risk is a loss of reputation. The protection of our reputation is therefore of paramount importance in all of our work.

Question 8 Would you find it useful if the total direct and indirect tax contribution by UK business to the UK economy was clearly defined and reported?

30. We believe that there needs to be more transparency and analysis of the UK businesses' tax contributions and this would be a useful statistic. It would make sense to include the figure in the HMRC annual report but this is not likely to be widely read. We see no reason why it should not be included on HMRC's website and/or included in information accompanying the company tax return.

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Question 9 Sarbanes-Oxley is rapidly becoming a ‘gold standard’ in compliance. On a scale of 1 to 5 how relevant is compliance with Sarbanes-Oxley to your group?

31. Our experience is that Sarbanes Oxley is a very relevant issue for many members with US interests. It appears to be increasing the compliance burdens and costs of doing business, but it is too early to tell whether these increased costs are matched and exceeded by improved investor confidence.

Question 10 Please indicate which, if any, of the following would encourage your group to share its tax systems, internal controls, audit reports or Sarbanes-Oxley documentation with HMRC?

32. We suspect that business would be reluctant to disclose such data with HMRC. Businesses will need to be satisfied that it will lead to lower compliance costs and less risk of disputes with HMRC. HMRC would also need to share relevant data with the business, for example any risk assessments
33. We would be delighted to discuss these issues further at a meeting, if that would be helpful.

FJH
20 December 2005