ICAEW
REPRESENTATION 70/24

BUSINESS TAX ROADMAP

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This text is based on a letter sent from Frank Haskew, Head of Tax, ICAEW, to James Murray MP, Exchequer Secretary to the Treasury.

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The letter covers:

- Corporation tax, and in particular:
  - Clarity, certainty and cost effectiveness of R&D tax relief;
  - Using capital allowances to support capital investment;
  - Improvements in advance rulings and clearances;
  - Supporting tax compliance by small and medium-sized businesses; and
  - Reform and simplification of international taxes.
- Simplifying and expanding the Enterprise Investment Scheme;
- Employee ownership trusts and employee benefit trusts;
- Simplifying the VAT regime;
- Modernising the business rates regime;
- Employment taxes and status; and
- Using the tax system to meet net zero.

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KEY POINTS

1. ICAEW welcomes the government's plans to publish a business tax roadmap. We also welcomed the opportunity to participate in the business tax roadmap roundtable hosted by the Exchequer Secretary on 12 September and we look forward to working with the Minister and his officials as this roadmap is developed over the coming months. Our comments below and in the attached appendix reflect the roundtable discussion and build on our representations in advance of the budget.
2. On 3 September, the Chancellor confirmed to MPs that "at the Budget the government will be outlining a tax road map for business to offer the certainty that encourages investment and gives business the confidence to grow". We agree that certainty and confidence are key objectives to meet if the roadmap is to have the intended impact of supporting growth in the UK economy. We have therefore focussed our suggestions below on changes and commitments that would support the certainty and confidence that businesses need to invest in, for example, machinery, premises, employment and training. We would also like the roadmap to set out how business taxation can be used to support the UK's transition to net zero.
3. ICAEW accepts that the government will not want to constrain its ability to react to external events, but it hopes that as a broad principle, the roadmap will set out how the government might react to external events. This is key for delivering certainty and enabling businesses to undertake scenario planning to invest with greater confidence.
4. ICAEW also welcomes the move to one fiscal event per year (Manifesto page 31). This should have the desired effect of giving 'due warning' of changes. Any policy proposal whether in a Budget or otherwise, also needs to recognise the time needed to update and test software and other administrative systems used by HMRC and businesses to implement these changes.
5. We understand that the roadmap will focus on corporation tax. Our recommendations therefore focus on this tax. However, we believe it is important not to lose sight of the wider tax landscape that impacts on businesses. A narrow focus on one particular tax risks missing a big opportunity to look at the business tax landscape as a whole and how the various taxes that businesses pay interact with each other. We believe that greater certainty in these areas would support the government's growth agenda and reduce costs for business. We have therefore included further recommendations in these areas towards the end of this document.

CORPORATION TAX

Clarity, certainty and cost effectiveness on R&D tax relief

6. We welcome the government's commitment to maintaining the current structure of R&D tax relief over the next parliament, which we believe will provide stability and certainty. We also recognise that the regime has been the target of significant levels of fraud and that HMRC must take action.
7. We have shared a detailed briefing with Treasury Ministers and HMRC to outline ICAEW's concerns about HMRC's response to fraud and error – in the form of its current 'volume-

based' compliance strategy – and the disruption and cost that approach is causing to many businesses undertaking genuine R&D activities. As a result of our briefing, we are having constructive dialogue with HMRC officials, which we welcome. There is a need to review HMRC's approach to tackling fraud and error in the regime as a matter of urgency to ensure that genuine claimants are not deterred from making claims, but that HMRC can properly risk assess and target dubious claims for relief.

8. In addition, we believe that an overhaul of the government's guidance on R&D tax relief, along with a commitment to update the guidance regularly to reflect new technologies, will help to embed the merged R&D relief rules. This guidance needs to be developed in consultation with businesses and advisers to reflect real-life examples of qualifying R&D projects across a range of industries.

Using capital allowances to support capital investment

9. A review of this area would help to support the government's growth and net zero ambitions. Simplification and certainty are key to maximising the investment incentive these allowances provide. Therefore, the commitment by the government to retaining full expensing and the £1m annual investment allowance are welcome. However, a review of the scope of the allowances would also be valued (including short and long-life assets and structures and building allowances).

10. There is, for example, an urgent need to move forward on the work on leased assets begun by the previous government, given the significant impact the leasing industry has on the UK economy. Consideration should be given to whether tax relief should be available for certain types of expenditure that does not currently qualify for either a revenue deduction or a claim for capital allowances. Examples include expenditure on feasibility studies and land preparation. Such costs tend to be significant in implementing sustainable energy projects (eg, wind farms as highlighted in the Upper Tribunal decision of Gunfleet Sands Ltd & Ors v R & C Commrs [2023] UKUT 260 (TCC)). Such measures would therefore contribute to the government's net zero objectives.

Improvements in advance rulings and clearances

11. ICAEW welcomes the government's commitment to trialling the greater use of advance rulings and clearances for major investment projects and identify areas where rulings and clearances could be beneficial, and supports the recommendations made above on capital allowances.

12. Alongside this, the government should consider whether all of the motive defence and purpose tests written into legislation are still required and are effective. When these were last reviewed in 2009 as part of the anti-avoidance simplification review, the tax legislation contained over 200 such tests with a wide variation in the detailed design. ICAEW supports properly targeted anti avoidance legislation, but these tests are a high cause of uncertainty for many ordinary business transactions, including the need for clearances (for example the transactions in securities rules, share exchanges, reconstructions and demergers) and can interact directly with business restructuring, refinancing and funding requirements.

13. The UK has had a general anti abuse rule since July 2013, and we would be happy to help in considering whether the anti-avoidance rules can be simplified without losing their ffectiveness.

Supporting tax compliance by small and medium-sized businesses

14. HMRC's Measuring tax gaps report for 2024 shows that the overall tax gap is on a downward trend. However, the tax gap for small businesses is increasing and in the 2022/23 tax year now stands at £24.1bn, equal to 60% of the overall tax gap and up from 44% of the overall tax gap for 2018/19. The tax gap for small businesses corporation tax is 32.2% of the theoretical corporation tax liability for that population, or £10.9bn in the 2022/23 tax year. A particularly concerning development is that the corporation tax gap for small businesses has been increasing steadily since 2011/12 and is considerably higher than the equivalent tax

gaps for mid-sized and large businesses. One of the policy objectives of the Making Tax Digital programme is to reduce the small business tax gap. However, as it will only apply to income tax it does not target the growing problem of the small business corporation tax gap.

15. The government needs to analyse what is causing this trend and clearly set out how it plans to help businesses comply with their obligations. As a professional body with many members who advise small businesses, we would like to work with government and HMRC to better understand the components of the small business tax gap and how we might support HMRC's efforts to reduce it.

Reform and simplification of international taxes

16. The UK tax rules relating to international tax matters have become increasingly complex over the past few decades, especially over the past ten years. We understand the need for the UK to align with the outcomes of the OECD's Base Erosion and Profit Shifting (BEPS) project and the inevitable complexity of the model rules agreed between the participating territories. However, we believe that there is considerable scope for simplification in this area.
17. For example, the pillar two rules (known as the multinational and domestic top up taxes in the UK) are perhaps the most complex international tax systems ever developed. While the rules are already substantially enacted in the UK and apply to current accounting periods of many groups, there is a significant amount of complexity and uncertainty inherent in the rules that businesses are grappling with.
18. We understand that the multinational and domestic top up taxes needed to be written in accordance with the OECD's model rules. We therefore recommend that HMRC continues to refine its guidance to assist businesses that need to comply with these rules.
19. In addition, and further to the point made above on advance rulings, the government could begin a review of existing anti avoidance measures (eg, controlled foreign companies, diverted profits tax, etc) with a view to repealing those that tackle the potential avoidance that pillars one and two and other more recent measures were designed to combat.
20. The government should also consider reforming the corporate interest restriction (CIR) rules, which cause a significant administrative burden for businesses beyond those it was originally intended to apply to. This is due partly to the increase in interest rates since the rules were enacted. Increasing the de-minimis £2m threshold (which has not been indexed since it was introduced in 2017) could help to bring many businesses out of the regime. Other administrative elements of the regime could be reformed, such as better aligning the filing deadlines and administration of the regime with the corporation tax return filing process.
21. Finally, section 71, Finance Act 2020, says that the Treasury must, before the end of 2025, conduct a review of digital services tax (DST) and prepare a report of the review. Companies subject to DST would welcome clarity on the future of that tax considering the protracted international negotiations on pillar one.

OTHER TAXES AFFECTING BUSINESSES

Simplify and expand the Enterprise Investment Scheme

22. The Enterprise Investment Scheme (EIS), established 30 years ago, has been one of the successes in attracting capital into the UK's businesses, making this country a more attractive destination for investment. Reform of venture capital tax reliefs could make them even more effective in encouraging investment by benefiting a wider range of companies, making them simpler to administer for HMRC and easier to understand by companies looking to raise funds.
23. We welcome the recent announcement of the extension of EIS and the Venture Capital Trust (VCT) regime by 10 years to 2035. Since its introduction in 1994, £41bn has been invested through EIS. The Treasury Committee in its Venture Capital inquiry heard that "EIS, SEIS and VCTs are internationally competitive schemes that attract investors, which in turn has provided billions in financial support to start-ups and growing businesses". In its evidence,

HMRC noted that these reliefs “improved business performance and bridged a funding gap that would otherwise emerge”.

24. Like the R&D regime, ICAEW members are reporting that HMRC is taking a more unhelpful approach to reviewing applications for advance assurance under EIS and before issuing EIS compliance statements. This undermines certainty and increases business burdens and compliance costs. The increased compliance costs means that there is effectively a de minimis on EIS fundraises that impacts many early-stage fundraising rounds. The existing approach needs a rethink.

Employee ownership trusts and employee benefit trusts

25. A consultation document was published in 2023 setting out proposed changes to the taxation treatment of these arrangements. The proposed changes were broadly designed to ensure that beneficial ownership of a company passes to the employees when legal ownership is transferred to the trust, as well as reducing the possibility of these arrangements to be used for tax avoidance purposes. To remove uncertainty and encourage greater take up of these arrangements in genuine employee take-over arrangements, we urge the government to consider the responses received to the consultation document and move forward with the proposed changes where they received broad support.

Simplify the VAT regime

26. VAT was introduced in the UK in 1973. Over half a century later, a comprehensive review of this tax is overdue. Committing to a review of the VAT system could appraise opportunities for simplification to deliver administrative efficiencies to boost activity and promote growth. ICAEW has been looking at the various options for reform and would be happy to discuss further.

27. The Office of Tax Simplification 2017 review should have been the start of a process to simplify VAT but far too few of its recommendations were taken further. Consideration should be given to how VAT could be made less complex to provide certainty and reduce costs for both business and HMRC.

Modernise the business rates regime

28. The current business rates regime is not conducive to a mission for economic growth. It creates a distorted playing field that often penalises growth and investment in new, more productive equipment, expansion in premises or development of derelict sites. It is important that the government sets out soon its plans to provide greater certainty for businesses.

29. The 2019 Treasury Committee inquiry Impact of Business Rates on Business concluded that “government must explore alternatives to address their negative impacts”. Although the subsequent Treasury Business Rates Review has built on this inquiry, further work is required, and the publication of the roadmap provides an opportunity to announce a start to this work. In ICAEW’s view, there is also a timely opportunity to optimise the system by better use of data and technology, which can improve efficiency while also mitigating disincentives for businesses to invest into local communities.

Employment taxes and status

30. Employment status is difficult to determine in the UK and such difficulty hinders growth.

31. Employment status for tax is also inextricably linked to the tax rate differentials that vary depending on both employment status and business form. The Public Accounts Committee concluded that “the complexity of the rules and perceived risk to hiring organisations of failing to comply with them could lead to changes in behaviour by both workers and hirers”.

32. Many disputes that arise between businesses, individual workers and HMRC necessitate recourse to the tax tribunals and the courts which is stressful, expensive and time-consuming. The previous UK government committed to work with stakeholders to address the problem. However, at that time, recovering from the pandemic took priority. The

Employment Status Consultative Committee, of which ICAEW is a member, has sent a letter to the Exchequer Secretary to the Treasury requesting that the Minister and officials work with stakeholders to formulate a solution that removes barriers to business growth.

Using the tax system to meet net zero

33. The UK tax system can play an important role in the transition to net zero and other green objectives by encouraging taxpayers to take sustainable action (like reducing their dependence on fossil fuels and making greater use of renewable energy). However, the government has not set out publicly a cohesive framework for supporting green investment and/or skills. We believe that this should form an integral part of the business tax roadmap.
34. From an international perspective, other countries have already introduced measures to attract and stimulate green investment (eg, The US Inflation Reduction Act). In addition, carbon taxes (eg, fuel duty and VAT on fuel) are already reducing as a share of tax receipts and therefore the government should form a credible plan as to where replacement tax revenues will come from in the long term