Representation from the Chartered Institute of Taxation
for Finance Bill Committee of the Whole House considering Finance (No.2) Bill 2023

Corporate Taxes

Corporation tax charge and rates: clauses 5 and 6
Capital allowances: clauses 7 to 9
Other reliefs relating to businesses: clauses 10 to 15
Part 3: Multinational top-up tax
Part 4: Domestic top-up tax

Chartered Institute of Taxation.

Executive Summary

Clause 7 - Full expensing

Welcome, but not as beneficial as it might at first appear due to it being time limited, only applying to expenditure on plant and machinery, and only applying to corporates

Clause 10 and Schedule 1 - R&D relief

Extending the definition of R&D is welcome but the ill thought out new compliance measures are not. The requirement for pre-notification of a claim will mean that many genuine claims will fall out of time, disproportionately affecting smaller companies. HMRC should pause and focus on current shortcomings in terms of compliance activities and enquiries etc.

We have a particular concern that the wording of a new power for HMRC to remove a claim for R&D relief from a tax return could be wider in scope than suggested, enabling HMRC to reject claims without taxpayers having any of the normal rights of appeal. We suggest an amendment to address this.

Part 3: Multinational top-up tax and Part 4: Domestic top-up tax

These measures to implement internationally agreed rules in relation to international corporate tax are very complicated and will place large compliance burdens on taxpayers and HMRC. We are doubtful they will raise as much as the UK government suggests, and there remain doubts as to whether some important countries will adopt them. Nevertheless, an international consensus is still preferable to competing unilateral measures and accompanying retaliation.

1 Corporation tax charge and rates: clauses 5 and 6

1.1 Clause 5 (Charge and main rate for financial year 2024) sets the main rate of corporation tax at 25% for the financial year 2024 (the rate has already been set at 25% for the financial year 2023 in Finance Act 2021). Each financial year for corporate tax begins on 1 April.

1.2 Clause 6 (Standard small profits rate and fraction for financial year 2024) sets the rate of the small profits rate at 19% for financial year 2024, and the marginal relief fraction at 3/200ths. The small profits rate was introduced by Finance Act 2021 to take effect from 1 April 2023 for companies that have profits of less than £50,000. It is set at 19% to maintain the level of corporation tax for the smallest companies.

2 Capital allowances: clauses 7 to 9

2.1 Capital allowances allow certain capital expenditure to be deducted when calculating a business's taxable profits. There was a consultation on *Potential Reforms to UK's Capital Allowance Regime*[1] last year. In our response we welcomed the review and said that we hoped that the result of it would be changes to the UK capital allowances regime that bring stability to the tax system and a sustainably supportive treatment of business capital investment for business income and corporation tax purposes.

2.2 Unfortunately, the changes to the capital allowances regime in the Finance Bill do not deliver this stability for all businesses. This is a missed opportunity because businesses require consistent levels of relief to help them plan and grow. The overwhelming feedback that we receive in relation to encouraging investment, and ensuring that the UK is a more attractive place for business, is that stability and certainty is more important to businesses than any particular rate of relief.

2.3 We also encouraged the government to use the opportunity of the review to decide on their longer-term strategy in relation to business investment and capital allowances, but this has not materialised. There is still no clarity around what business investment the government wishes to encourage, and the changes introduced by the Finance Bill do not have any clear policy aims around what capital expenditure is being incentivised. (The 'full expensing' regime is targeted at 'plant and machinery' with various exclusions for most cars, leased assets, so-called 'special rate' assets (see below) and structures and buildings that do not meet the tax definition of plant and machinery: these distinctions reflect long-standing tax classifications and in some cases concerns about avoidance but not, so far as we are aware, any recently considered view as to national priorities for investment.) We said that the government should consider a broader reform of some aspects of the capital allowances regime, and other tools. For example, the government should consider introducing some form of 'above the line relief', upfront grants or subsidies for particular types of expenditure and an ability for loss making companies to surrender allowances for a payable tax credit, similar to the SME R&D tax relief scheme. The review also provided an opportunity for the government to ensure that capital allowances are given to assets and expenditure that will help achieve the government's broader policy objectives, such as levelling up, reduction in CO_2 and energy efficiency (net zero), promoting innovation and high tech (high productivity) R&D industries, or improved and increased house building. This has not happened.

'Full expensing'

2.4 Clause 7 (Temporary full expensing etc for expenditure on plant or machinery) introduces new temporary first year allowances which are unlimited for 'main rate' qualifying expenditure on plant and machinery and 50% for qualifying expenditure on special rate assets[2] expenditure. These allowances have effect for expenditure incurred on or after 1 April 2023 but before 1 April 2026.

2.5 Currently, for expenditure on the provision of plant and machinery, writing down allowances are 18% per year for main rate expenditure and 6% per year for special rate expenditure. This measure provides for 100% first-year allowances for main rate expenditure (known as full

[1] The consultation document and the CIOT's response to it can be found at [Potential Reforms to UK's Capital Allowance Regime (tax.org.uk)]

[2] Special rate assets are those defined as such for purposes of capital allowances. These assets are usually entitled to a lower 6% special rate writing down allowance, as opposed to the 18% main rate writing down allowance. These assets include, for example certain building fixtures or integral features of buildings, such as electrical systems - wiring, lighting, heating or ventilation systems – and long life assets – equipment with an expected business life of 25 years or more

expensing) and 50% first-year allowances for special rate expenditure, subject to certain exclusions. It is intended to provide an increased incentive to invest in plant and machinery through providing higher rates of relief in the period the expenditure is incurred.

2.6 The full expensing measure in the Finance Bill is in essence an unlimited annual investment allowance (AIA) for all companies. It is a generous relief for the largest companies whose capital expenditure on plant and machinery is in excess of the limit for the AIA (currently £1m). It gives the greatest simplification to the business tax system out of all the options considered by the Government in their review last year. However, it lacks the ability to target incentivisation at particular types of capital investment or business in line with the government's overall policy objectives. Also, it is hard to predict the extent to which it will incentive investment, not least because of its significant exclusions and limitations:

- it is time limited
- it only applies to expenditure on plant and machinery (with further exclusions from that)
- it only applies to corporates

2.7 The most significant drawback of the full expensing measure is its temporary nature. Notwithstanding the Chancellor's expressed desire to continue it beyond the three years being legislated for, if resources allow, companies may still be reluctant to rely on it in their long term planning for capital investment. Thus the more generous relief will largely reward investment that was going to happen anyway, and it may be less effective than anticipated in its stated aim of stimulating additional investment. It is also not helpful that, despite the consultation on the capital allowances regime in Spring 2022, the announcement of full expensing was only made at the Budget on 15 March, only 17 days ahead of coming into force.

2.8 It is our longstanding view that there has been too much tinkering with rules and rates of capital allowances. Frequent changes more often than not bring complexity and uncertainty, and undermine investor understanding of, and confidence in, what is on offer at any one time. It is unfortunate, therefore, that the 'headline' new measure of full expensing is temporary in nature. This leaves unresolved the question of what is the ongoing permanent level of support through the tax system for corporate capital investment.

2.9 As the full expensing measure only applies to expenditure on plant and machinery, it will not help businesses that invest in things other than plant and machinery (for example, structures and buildings or mineral exploration and extraction). In addition, it will still be necessary to use case law to distinguish between plant and machinery and, say, buildings. There will, however, arguably be some simplification as, for example, if an item is considered plants less will turn from a tax perspective on correctly determining whether the expenditure on it is capital or revenue.

2.10 The final significant restriction in relation to the full expensing measure is that it is only available for companies. This means that it will not benefit or incentivise large businesses that are not incorporated. This would include, for example, partnerships of individuals such as farming partnerships, that may have significant capital investment in equipment such as large dairy facilities, and accounting or law firms that may wish to invest in their IT infrastructure. If there are individual partners, the partnership does not pay corporation tax and so cannot access the full expensing relief. There is not an obvious policy reason for excluding these businesses.

2.11 In addition to the impact of the measure being temporary in nature, it is unlikely to be helpful to project companies that are loss making in the first few years of a long-term project. This is because claiming the full expensing relief will only increase the amount of losses that will then be restricted in subsequent years as a result of the corporation tax loss restriction rules.

Annual investment allowance (AIA)

2.12 Clause 8 (Annual investment allowance to remain at £1M beyond temporary period) puts the £1m AIA onto a permanent footing. The AIA was temporarily increased to £1m from 1 January 2019 by Budget 2018 for an initial two-year period that has subsequently been extended to 31 March 2023.

2.13 This permanency for the AIA is welcome. The AIA simplifies the tax and capital allowances computations of businesses within its limits. We have previously commented on the complications and cliff edges that have arisen over recent years as a result of the chopping and changing in the level of the AIA. The government should also consider broadening the expenditure that qualifies for the AIA to provide further simplification for smaller businesses.

Electric vehicle charge points

2.14 Clause 9 (First-year allowance for expenditure on electric vehicle charge points) extends the availability of first year allowances for expenditure on plant or machinery for electric vehicle charging points for two years, so that the 100% first year allowances is now available until 31 March 2025.

2.15 This further extension until 2025 is intended to provide continued support for the use of electric vehicles to promote the uptake of cleaner vehicles. The extension also more closely aligns the period in which this tax relief is available with the first-year allowances for zero emission cars and goods vehicles, which are also due to end in 2025.

2.16 Given the government's net zero targets, it is difficult to see why these reliefs around electric vehicles are temporary in nature.

3 Other reliefs relating to businesses: Research and development (R&D)

3.1 R&D relief is a long-standing form of government intervention into economic activity that is supported throughout the business world.

3.2 Clause 10 (Relief for research and development) and Schedule 1 introduce changes to the R&D tax relief for small or medium sized companies ('SME tax relief'), and to R&D Expenditure Credit ('RDEC'), which is mainly claimed by larger companies, to widen qualifying expenditure to include data licenses and cloud computing services. It also introduces new compliance measures. The changes generally have effect for accounting periods beginning on or after 1 April 2023, but the requirement to provide additional information with a claim has effect for claims made on or after 1 August 2023.

3.3 The main compliance changes are:

- The requirement to make a claim notification of an intention to make an R&D claim in a shorter time frame than the period allowed for the making of an actual R&D claim; and
- A new requirements for claimants of SME R&D tax relief or RDEC to provide additional information to support their claims

We understand that these measures are aimed at tackling error and fraud. We are supportive of the government taking action to do this, but we are doubtful that the measures will be successful in this regard.

General comments

3.4 The way the UK is currently implementing changes in relation to R&D (including changes in HMRC practice and interpretations of legislation alongside openly pursued consultations and legislative changes) is making things worse for investment that is happening in the short to medium term. The government continues to state its policy aim of encouraging innovation and achieving the ambitious target of total investment in R&D rising to 2.4% of UK GDP. Unfortunately, most of the changes in the Finance Bill do not support this policy aim.

3.5 The current approach of piecemeal and rapid changes is harmful to the additionality of R&D relief. The constant changes will discourage marginal investment, making it more likely that relief will be given to investment that would be happening anyway, rather than encourage companies to choose the UK as a location during the decision making process on whether and where to invest. The government says that it continues to recognise the importance of R&D tax relief in the context of the UK's international competitiveness. In this regard, we suggest that the UK is looking increasingly less competitive in light of recent international developments[3] and the recent and anticipated changes lead to uncertainty, which is one of the biggest blockers to investment.

3.6 The government confirmed its commitment to supporting SME R&D in the recent consultation on a single scheme for R&D[4]. However, the disproportionate impact on smaller companies of these new compliance measures does not seem to be recognised. Our fear is that they will make complying with the requirements of R&D tax relief too burdensome and too costly for SME companies - deterring them from claiming and, ultimately, the overall impact will be to discourage R&D.

3.7 In addition, the introduction of these measures at this time is surprising in light of the ongoing review into R&D tax reliefs and, in particular, the consultation mentioned above on whether the two R&D schemes should be merged into a single scheme. The outcome of this consultation will likely result in further changes in short succession, which will be disruptive for businesses.

Claim notification

3.8 Part 1 of Schedule 1 to the Finance Bill sets out the requirements for the claim notification. This measure mandates that companies must inform HMRC of their intention to make a claim for R&D tax relief using a new digital form (broadly) if they have not claimed R&D tax relief in the previous three years.

3.9 The House of Lords Finance Bill Sub-Committee considered all of the compliance measures in the Finance Bill at the end of last year, publishing a report in January 2023[5]. The sub-committee concluded (in the introduction to the report) that: '*We consider that legislative reforms of this nature will not be effective in isolation and that improvements to HMRC's*

[3] In February 2023 South Africa announced an effective 125% tax deduction for R&D, and there are similar measures being introduced in other countries, for example Singapore and Chile. Also the Inflation Reduction Act of 2022 in the US, and the response to it from the EU, will have an impact in terms of international competition.

[4] [R&D Tax Reliefs Review: Consultation on a single scheme - GOV.UK (www.gov.uk)]

[5] [House of Lords Report: Research and development tax relief and expenditure credit]

compliance capability are also required. This includes a more focused and targeted approach to identifying suspect claims, greater expertise and potentially more resource.'

3.10 In particular, we agree with the report's conclusion regarding the requirement to make a claim notification, that this will be '*uniquely onerous, without any direct precedent within the tax system. It risks companies being unable to make legitimate claims, while its benefits in countering abuse are questionable*.' (paragraph 85).While we acknowledge that bad behaviour by some firms claiming R&D tax credit specialism is a problem, we suspect that 'ambulance chasing' activity will simply shift in time from encouraging maybe dubious claims to encouraging protective and speculative pre-notifications. The real solutions to this issue lie in more graduated HMRC compliance responses in the R&D tax credits area, and in reviving the government's largely stalled agenda on raising standards in the tax services market.

3.11 In our view the claim notification measure is poorly targeted because, although it will prevent some dubious claims, it will mean that many genuine claims will fall out of time. There will be significant collateral damage from the measure, disproportionately affecting smaller companies. The proposal will exacerbate an unfairness that can arise between taxpayer companies that undertake R&D activities, based on whether or not they have an awareness of the tax relief rules at the appropriate time. Companies that employ tax advisers on an ongoing basis will be at an advantage to those that do not. As noted above, it is difficult to see how making it harder to claim R&D tax relief will help deliver the government's overall policy of encouraging R&D, and delivering the overall additionality benefits of the schemes.

Additional information required

3.12 Paragraph 13 of Schedule 1 of the Finance Bill introduces a new obligation on companies to provide a digital additional information form with their claims. This requirement will apply to all claims made on or after 1 August 2023.

3.13 We recognise that some aspects of the additional information that will be required could be useful to HMRC, if they have the resource to properly capture the information and use it effectively in triaging risk. However, the introduction of the measure has been rushed without considering all of the practical difficulties of the proposed new digital forms. There will be a significant additional compliance burden for all companies and duplication of effort with regard to R&D tax relief claims, not least because the new digital form does not interact with the actual making of the claim for R&D tax relief (in the corporate tax return CT600 and existing additional form CT600L).

3.14 There was no consultation on the requirement to submit an additional information form, and, therefore, no opportunity to discuss with HMRC the practical implications, nor input on the design elements of the digital form. The regulatory impact assessment published with the Spring Budget says that '*This measure is expected to have significant impact on the administrative burden of approximately 90,000 businesses claiming R&D tax reliefs.*[6]'. Notwithstanding this, it is not clear that the government has fully considered the costs and consequences of enforcing this measure. The compliance burden will be significant for SMEs and micro businesses in particular that do not routinely capture the specific project and company costs that will be required to produce the information, giving rise to a significant additional administrative burden. In addition, the Budget announced that the new online additional information form is going to have a start date of 1 August 2023, which is earlier than previously expected. This earlier implementation date will be challenging for advisers, who will have to ensure that their systems are able to deal with this new compliance measure

[6] Research and Development Tax relief reform changes - GOV.UK (www.gov.uk)

and that tax compliance teams are properly trained etc. Although there have been some online demonstration sessions by HMRC of draft versions of the digital form, the actual form was only made available on 1 April 2023.

3.15 There are a multitude of practical issues that have been raised with HMRC, but are not yet resolved. These include:

- issues around how the digital form can be managed when a company has more than one tax adviser (for example a main corporation tax agent, but they receive specialist advice in relation to R&D),
- how the information in R&D reports that are already produced can be utilised in relation to the additional information form to minimise the compliance burden, and
- as mentioned above, how the information provided will link with the overall corporate tax return.

Full guidance from HMRC clarifying the issues is awaited. It would be helpful if the minister could say during debate when this will be published.

3.16 Finally, we are concerned that if the requirements of the additional information are not carefully communicated by HMRC, this new compliance measure could cause confusion and may result in a lower standard of behaviour. If companies are undertaking a large number of R&D projects, the new requirement to provide additional information only applies in respect of a proportion of them. We think that confusion may arise because companies (and some advisers) may assume that detailed information is not required in respect of the remaining R&D projects that have been undertaken by the company, and for which tax relief is being claimed. However, this is not correct: HMRC will be entitled to request further information in respect of all of the projects that have been undertaken under their enquiry powers. HMRC need to make it very clear that that the requirement to provide additional information in respect of some projects does not negate the obligation on a company to ensure that it has sufficient information in respect of all of its R&D projects to support its claim for tax relief.

Amendment to the legislation suggested

3.17 In addition to our general and practical concerns about these new compliance measures, we also have a specific concern with the wording of a new power for HMRC.

3.18 Paragraph 14 of Schedule 1 of the Finance Bill introduces a new power for HMRC to remove a claim for R&D relief from a corporation tax return when an officer of HMRC 'reasonably believes that the claimant company failed to comply with a requirement for making a claim'. A new paragraph 83EB is inserted into Schedule 18 to FA 1998. The problem with this new power is that there is no right of appeal against a decision of HMRC made pursuant to it. There is merely a right for the taxpayer to make representations.

3.19 It is our understanding that this new power is only intended to be available to HMRC in relation to failure to comply with the new compliance measures being introduced by the Finance Bill. That is to say that HMRC can only remove an R&D claim from the company tax return in the event of a failure by the company to either make a claim notification or submit the additional information required. In this regard we note that the Explanatory Notes to the Finance Bill say about this measure: 'This will allow HMRC to reject claims which have not been the subject of a claim notification, or where the additional information requirement has not been fulfilled.'

3.20 However, it is not clear that the wording of the new legislation itself is limited in this way. Although the new paragraph 83EB(1)(a) refers to 'a requirement relating to the making of the claim' (emphasis added), which arguably limits its application to the administrative and compliance measures linked to the making of a claim, as drafted it could also be construed as referring to any requirement, or condition, that must be satisfied in relation to an R&D claim, all of which are pertinent in the 'making' of an R&D claim. The 'making' of a claim could, for example, arguably include a reference to the requirement that expenditure included within it must be on R&D as defined in law, or must not be subsidised or contracted out etc. Matters such as these can at times be contentious between HMRC and the taxpayer.

We suggest that the legislation could helpfully be clarified by adding some additional wording into the new paragraph 83EB(1)(a) to specifically refer to the new compliance provisions, as shown underlined below, and deleting that wording shown as struck out:

(a) reasonably believes that a claimant company has failed to comply with the requirement to make a claim notification pursuant to either section 104AA, section 1045A or 1054A of CTA 2009 (as appropriate) or failed to provide the additional information as required by paragraph 83EA ~~a requirement relating to the making of the claim~~ (and accordingly that the claim has been made in error), and

3.21 The amendment would read –

Schedule 1, page 280, line 32, leave out "a requirement relating to the making of the claim" and insert "the requirement to make a claim notification pursuant to either section 104AA, section 1045A or 1054A of CTA 2009 (as appropriate) or failed to provide the additional information as required by paragraph 83EA"

Explanatory statement: This amendment would make clear that the power to remove a claim for R&D relief from a corporation tax return is only available to HMRC where a company has failed to make a claim notification (required pursuant to Part 1 of this Schedule) or to submit the additional information (required pursuant to paragraph 13 of this Schedule).

3.22 Of course, we do not dispute that all of the other requirements for a claim for R&D must be met. But, as a matter of policy, tax disputes should be dealt with through the normal enquiry framework and ultimately be resolved in the tax tribunals. In our view, introducing new powers in this manner without a right of appeal (which follows similar drafting in relation to accelerated payment notice rules) is unwelcome. It means that the only recourse for a taxpayer that disagrees with HMRC's decision would be judicial review which is more costly for the taxpayer, and HMRC, and would further clog up an already overburdened court system. In our view proceeding in this way, without any right of appeal, is unwelcome even in relation to circumstances of non-compliance with administrative requirements around the 'making of the claim'. But it is definitely not appropriate for more substantive disputes in relation to the actual claim itself, and the legislation should be clear in this regard.

3.23 Without an amendment such as this we think the legislation could effectively be a trojan horse for a new HMRC power to reject R&D claims without the taxpayer having any of the normal rights of appeal.

Looking ahead

3.24 As noted above, the government consulted on a single scheme for R&D tax relief earlier this year. At the Spring Budget, the government said that it has not yet decided whether to merge the two different R&D schemes. However, it was also announced that draft legislation on a single scheme would be published for technical consultation in summer 2023, which suggests its mind is already made up.

3.25 The Budget also announced that the government will legislate in a Finance Bill 2023-24 to provide additional R&D tax relief for eligible R&D intensive SMEs. Although this additional relief is welcome for those that will qualify for it, extraordinarily it applies from 1 April 2023, even though we have not yet had sight of the rules. Draft legislation will be published in summer 2023. If, as was suggested in the consultation on a single scheme, the new, merged scheme comes in in April 2024, then the higher rate for loss-making R&D intensive SMEs will only have been in place for one year, unless the government maintains the higher rate in a merged scheme.

3.26 All of these changes indicate that there is little long term policy thought or planning around the strategy or direction of R&D tax relief. We suggest that the government should pause and take the time to reset their thinking around R&D tax relief. Time should be taken to address the concerns set out in the Lords' report about the current challenges of the operational aspects of the tax relief and compliance activities being undertaken by HMRC.

3.27 As noted above, the way that the R&D SME scheme is currently being operated is making it increasingly difficult for SMEs. In particular there has since Autumn 2022 been a significant increase in the number of enquiries being opened by HMRC into smaller claims for R&D tax relief. While we support HMRC in efforts to ensure that tax relief is being correctly claimed and awarded, the manner in which the enquiries are being conducted by a team within HMRC that focuses on volume compliance has proved in many cases to be disproportionate and out of kilter with the manner in which HMRC undertakes to conduct enquiries in both the Taxpayer Charter and their manuals[7]. HMRC have recognised some of the issues and we would encourage them to continue to focus on the necessary capability build, as the current situation is damaging to the overall perception of the tax relief and is undermining the overall policy aim of encouraging R&D.

3.28 In any event, the mooted date of a change to a single scheme in April 2024 is too soon from a practical perspective. At the very least, time must be allowed to ensure that the new rules are fully published, and the detail of what will be required from companies is fully available, in good time before the commencement of a new regime (unlike the unsatisfactory position with regard to the changes coming into effect from 1 April 2023, in respect of which the detailed rules were very late in being made available). It is important that changes are managed in an efficient manner and well communicated in conjunction with transitional rules which minimise commercial disruption. The government should be encouraged to act on the recommendations made by the Lords in their report. These will remain relevant in relation to any new, single scheme. In particular, the perceived issues around HMRC's compliance activities will not be solved by a single scheme.

Data and cloud computing

3.29 We welcome the changes to the definition of R&D that will permit relief in relation to expenditure on data and cloud computing. However, it is a missed opportunity that the overall definition of R&D for tax purposes has not formed part of the R&D tax reliefs review (that has been taking place since 2021). We suggest that a review of the current definition of R&D is undertaken by the new Department for Science, Innovation and Technology.

Other changes

[7] For example, onerous information requests with unreasonable time limits, HMRC refusing offers to speak to the company or their competent professionals about the R&D claim (which is a normal part of an R&D compliance check as per HMRC manuals), lack of due care and skill in the written communications that rely heavily on template wording.

3.30 We do not have any comments on the other amendments being made to the R&D relief schemes which address anomalous results.

4 Other reliefs relating to businesses: clauses 11 to 15

4.1 Clause 11 (Treatment of profits from patents etc: small profits rate of corporation tax) amends the Patent Box deduction formula to refer to 'applicable rate' rather than 'main rate' of corporation tax. This will ensure the formula remains accurate for companies paying the new small profits rate, those with profits of £50,000 or less, from April 2023.

4.2 Clause 12 (Energy (oil and gas) profits levy: de-carbonisation allowance) introduces a new investment allowance at a rate of 80% for oil and gas companies for investment in the de-carbonisation of upstream petroleum production activities.

4.3 Clause 13 (Museums and galleries exhibition tax relief: extension of sunset date) extends museums and galleries exhibition tax relief (MGETR) for a further two years, until 31 March 2026.

4.4 Clause 14 (Extension of the temporary increase in theatre tax credit etc) extends the temporary increased rates for theatre tax relief (TTR), orchestra tax relief (OTR), and museums and galleries exhibition tax relief (MGETR) for two years, until 31 March 2025. The rates have been set at 45% (for TTR and MGETR non-touring productions) and 50% (for OTR, and TTR and MGETR touring productions) since 27 October 2021. From 1 April 2025, the rates of relief drop to 30/ 35% respectively. From 1 April 2026, the rates will return to 25/20% respectively.

4.5 Clause 15 (Seed enterprise investment scheme: increase of limits etc) increases the limits that apply to company access and use of the Seed Enterprise Investment Scheme (SEIS) and the investment amounts on which individual investors can claim tax reliefs.

4.6 We do not have any specific comments on the changes being proposed by these clauses of the bill.

5 Part 3: Multinational Top-up Tax and Part 4: Domestic Top-up Tax

5.1 In October 2021 more than 135 countries in the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS) agreed a two-pillar solution to reform international tax to deal with the challenges arising from the digitalisation of the global economy, aiming to ensure that multinational enterprises (MNEs) pay a fair share of tax wherever they operate and generate profits.

'Pillar 1' involves a partial reallocation of taxing rights over the profits of MNEs to the jurisdictions where consumers are located. The detailed rules that will deliver this are still under development by the Inclusive Framework.

'Pillar 2' intends to ensure that MNEs pay a minimum rate of 15 per cent corporation tax (or their version of it) in every country they operate in.

5.2 The multinational top-up tax and domestic top-up tax introduced by Parts 3 and 4 of the Finance Bill is the first tranche of implementation by the UK of the agreed G20-OECD Pillar 2 framework. It is envisaged that additional law and significant additional guidance will be required to supplement this tranche as negotiations are continuing at the OECD on many technical and interpretive issues (the "Implementation Framework"), as well as mechanisms for qualifying each country's implementation for the purpose of other implementing countries' rules.

5.3 The principle behind the Pillar 2 rules is that where a group company in jurisdiction A has paid less than 15% tax on its profits, then jurisdiction B where there is another group company, higher up the ownership chain in the corporate structure, is expected to impose a 'top-up tax'.

5.4 This has the following consequences:

- It requires a new detailed definition of 'profit' for the purposes of calculating the effective tax rate. You cannot use existing definitions because each country has a different one. The clauses of the Finance Bill are intended to enact the new Pillar 2 definition into UK law for the purpose of calculating and imposing the top-up taxes in the UK.

- Every country is incentivised to impose a tax to take at least 15% of profits (as defined by the Pillar 2 framework) of companies in its jurisdiction. If it does not impose such a tax, the jurisdiction of companies higher up the ownership chain will. So, the country will forgo revenue but still suffer whatever loss of competitiveness is attributable to the tax, because tax on those profits will still fall due, albeit payable to another country. Essentially the UK government is responding by introducing the two top-up taxes envisaged by the Pillar 2 framework: one aimed to top up the tax on profits of companies outside the UK (the multinational top-up tax), and the other on profits of companies in the UK (the domestic top-up tax). (It is possible that companies in the UK will have paid a rate of less than 15% under Pillar 2 definitions, even if they have paid the higher UK CT rate on domestic UK definitions.)

- Each country also has an incentive to make it as clear as possible to the Inclusive Framework and to all the other countries, that it is effectively taxing companies within its jurisdiction to the required 15% level in accordance with the Pillar 2 rules. If this is doubted or disputed, other countries might seek to impose their own top-up taxes on group companies higher up the ownership chain. This is why the approach has been taken in the Bill of having two new taxes alongside all the UK's existing legislation, rather than of trying to integrate the OECD agreement by a series of changes to existing corporation tax law. There is no guarantee that that alternative approach would have been any simpler, and it would have made it harder to demonstrate to the OECD and others that we were imposing what the agreement required.

5.5 Because of these incentives, which began to operate once the concept of the Pillar 2 rules had been accepted by a critical mass of jurisdictions, we are doubtful that the UK will derive the large amounts of extra revenue suggested. Countries with corporation tax rates below 15% will be incentivised in the same way, and will likely introduce new, or increased, taxes of their own rather than leave 'money at the table' for the UK (or others) to pick up. Though there will likely be a more level playing field as a result.

5.6 We are not opposed to the introduction of a global minimum tax in principle. We have long advocated a multilateral solution to the tax challenges arising from the digitalisation of the economy in light of the increasing unilateral measures (and retaliatory actions) being taken by countries. Against that alternative, we have supported the work towards a multilateral solution and the two-pillar approach. However, it must be recognised that the scope and detail of the Pillar 2 (or Global Anti-Base Erosion (GloBE)) Rules – and, as a result, the multinational top-up tax that is the UK version of it - is vastly complicated and will create an enormous administrative burden for tax administrations and MNEs alike.

5.7 Throughout the process of developing the rules, we have been concerned that the desire to reach an apparently positive outcome to a timetable ran ahead of real resolution of the technical issues, casting doubt on whether we will achieve a workable set of rules that will result in a genuinely stable, reformed international tax system.

5.8 The Inclusive Framework published model legislation (Model Rules) for Pillar 2 in December 2021. Unfortunately, the speed at which the rules were developed led to significant challenges with the rules as published, with them leading to arbitrary and unsatisfactory outcomes in some cases. The Inclusive Framework has subsequently published Commentary, which provided further technical guidance on the rules, in March 2022, and Administrative Guidance in February 2023. Most recently, there have been consultations on the GloBE Information Return (GIR), which is intended to provide a standard form for consistent collection of information, and on tax certainty. All of these are important steps in the ongoing work in relation to Pillar Two. However, there are several important aspects of the rules outstanding and still to be developed, particularly around tax certainty and compliance/administration of the rules.

5.9 The UK published the first draft of its legislation in February 2022. Throughout the process of implementing the rules in the UK, the government's approach has been to follow the Model Rules, even if this leads to outcomes that do not appear to meet the policy objective of a 15% minimum tax on profits. We understand that the rationale for this is to ensure, so far as possible, the principle of consistency across the globe in respect of the GloBE rules. However, this also means that the outcomes embedded in the Model Rules have been incorporated into the UK rules, even where these are contrary to the broader policy aims of Pillar 2 (for example, give rise to double taxation).

5.10 However, notwithstanding this approach, it seems that some divergence in language, even if not necessarily in effect, is inevitable as jurisdictions take different approaches to drafting when implementing their domestic rules. This is why the focus on ways to achieve tax certainty so far as possible is very important. We have consistently said that the implementation of the GloBE Rules will require significant resource from national tax administrations, as well as, of course, from in-scope MNEs (and the OECD). Further resource will be one of the key challenges in achieving tax certainty. We encourage the UK government to commit to providing the additional resource that will be required. We also strongly encourage the UK government to advocate that dispute prevention and resolution mechanisms agreed in relation to the Pillar 2 rules should be binding on tax administrations.

5.11 As noted in paragraph 5.4, an important aspect of how the Pillar 2 rules work is that domestic rules such as those being introduced by Part 4 of the Finance Bill should be considered to be 'qualifying' by other jurisdictions. This will mean that these rules enable the UK to impose a minimum tax on MNEs head-quartered in the UK, rather than other jurisdictions imposing a top-up tax on these groups. It is intended that, in due course, whether or not domestic rules qualify will be 'peer reviewed' by an agreed mechanism operating through the Inclusive Framework. However, until such time as the peer review mechanism is agreed and in a position to be implemented, we welcome that the Inclusive Framework has confirmed that the UK's domestic top-up tax should be considered to be 'qualifying'.

5.12 We recognise and support the UK government's track record of leadership on international tax reform and it has continued in this role in terms of being an early mover in respect of implementing the Pillar 2 rules. Several other jurisdictions, as well as the EU have also confirmed their intention to implement Pillar 2 rules. However, there remains some doubt as to whether the rules will be implemented in several important jurisdictions. In particular, although the principle of Pillar 2 has been supported by the US administration (to the point that the minimum tax rate is regularly referred to as the 'Biden proposals'), it is not at all clear that the US will support the detailed negotiated package to implement the rules.

5.13 It may be helpful to press the minister during the debate on progress of adoption of Pillar 2 by other countries, and also on the progress of Pillar 1 negotiations. The UK Digital Services Tax is intended as a stopgap, to be abolished once agreement has been reached on the allocation of taxing rights internationally (Pillar 1). But with little sign of a breakthrough in those talks that will lead to any agreement that all major economies will be able to sign up to, there are concerns that this supposedly temporary tax (as a revenue tax it is a blunt instrument that cannot accurately represent the tax on the profits generated in the UK) could effectively become a permanent part of the UK's tax landscape. Are ministers concerned about potential retaliation from the United States – which feels the Digital Services Tax unfairly targets American companies – if agreement on Pillar 1 is not reached soon?

6 The Chartered Institute of Taxation

6.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT's comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

The CIOT's 19,000 members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

For further information, please contact:
George Crozier, CIOT Head of External Relations
gcrozier@tax.org.uk / 020 7340 0569

The Chartered Institute of Taxation
13 April 2023