Tax Services

Corporate Governance Code meets Tax Code of Practice

Executive summary

The publication, on 22 July 2015, of HMRC's consultation document on *'Improving large business compliance'* is an attempt to draw a bright line between acceptable and unacceptable tax behaviour. The measures under consultation include publication of tax strategies and the naming of a responsible board executive; both aimed at creating a clear link between good corporate governance and board accountability for an organisation's approach to tax risk and planning. There is also a voluntary Code of Practice (CoP) on Taxation, though banks will keep their existing Code. Furthermore, the consultation document includes the prospect of a 'special measures' regime for high risk businesses, leaving business in no doubt as to the severe reputational risks and financial consequences for the minority of businesses that continue to adopt aggressive tax planning strategies and fail to cooperate with HMRC.

Personal accountability by named board member for 'tax strategy'

With a main principle of the UK Corporate Governance Code being that boards are responsible for the maintenance of sound risk management systems, there has always been a link between good governance and an organisation's approach to tax planning. It is unsurprising, in the current environment, that HMRC is seeking to make this link explicit in the consultation document. What is surprising however is the inclusion of a requirement for an executive director to be named as having responsibility for signing off an organisation's tax strategy. It could be inferred from the proposal that the individual's name could form part of the published strategy, so as to reinforce executive board accountability. The rationale behind this comes from research commissioned by HMRC, which states that increased scrutiny of an organisation's approach to tax matters by the board discourages aggressive behaviours.

The naming of an individual with responsibility for tax strategy is an evolutionary step. This approach first appeared as part of the Senior Accounting Officer (SAO) regime in Finance Act 2009. Whilst the SAO regime imposes personal obligations and potential penalties on the SAO, the individual is clearly only notified to HMRC and does not have to be a board level executive. Whilst HMRC has stated that the SAO regime and this proposal are to be kept apart, bringing tax strategy and risk unequivocally onto the boardroom agenda may bring together the role of SAO and the director accountable under these proposals. Indeed, this may be a desirable outcome from both HMRC's and the organisation's perspective, ensuring a holistic approach is taken to tax governance, risk and compliance and reporting.

Building a better working world

Tax transparency – the next iteration

With almost two thirds of FTSE100 businesses now voluntarily disclosing tax information such as tax policies, tax principles and tax payment information, the proposed mandatory disclosure of an HMRC defined tax strategy would accelerate this trend and cover over 2,000 businesses.

However, the proposal is not only for publication of attitude to tax risk but also more granular disclosure of whether the group has a target Effective Tax Rate, what this is, and what measures the business is taking to maintain or reach this target. This, together, with a possible requirement to disclose compliance with a voluntary CoP, which defines acceptable behaviours as being those intended by Parliament (intentions that are not always clear), may be regarded by some as problematic.

SAO guidance issued in the last couple of years by HMRC to its Customer Relationship Managers (CRMs), has emphasised the need to communicate a tax policy throughout an organisation as part of an effective tax risk and control environment. In our experience, most large businesses that are likely to fall into this new publication regime, will, therefore, have taken steps to refresh or re-write their tax policies. However, these do not always contain the level and type of information and explanations that HMRC would like to see and organisations may have to look again at whether their tax policy or strategy document is suitable for publication, as well as considering how best to publish it.

Mind your conduct

The consultation document includes a proposed voluntary CoP on Taxation for Large Business. Should a business choose to sign up to the CoP, it will gain the benefit of being seen as adopting lower risk behaviours when being risk assessed by their CRM. HMRC will not publish details of those signing up to the CoP but has asked whether businesses should be required to publish whether they are or are not a signatory to the CoP as part of their publication of their tax strategy. Furthermore HMRC will make an exception for those organisations which make inaccurate public statements.

It will be interesting to see how this develops, bearing in mind the development of the Code of Practice on Taxation for Banks, which is also a voluntary code. In 2010 the Chancellor gave the major banks a limited time to sign up to the Code, subsequently publishing with some fanfare the names of the top fifteen banks who had duly voluntarily signed up. This was followed in 2014 by HMRC being charged with publishing an annual report listing groups or entities which have unconditionally adopted the Code at the date of the report as well as those groups or entities which have not adopted the Code and naming any groups or entities that HMRC considers has not complied with Code.

Organisations should, therefore, consider the long term view when formulating any response to the consultation and their willingness or ability to sign up to the CoP.

Entities governed by the Code of Practice on Taxation for Banks will not be part of the new CoP. They will, however, still be within the scope of the other proposals announced.

If there is no public disclosure of signatories to the new CoP, organisations that are content to sign up to the CoP may well seek to publicise this as a way of mitigating stakeholder concerns about tax risk. Inevitably, this means stakeholders may be left to draw their own (potentially erroneous) conclusions in respect of those organisations which remain silent. This emphasises the growing need for an organisation to take a more systematic approach to tax communications and to be clear about who it wants to communicate with on tax matters.

Managing reputational tax risk

The publication of this consultation document is another ratcheting up of the reputational risk profile of tax. Many stakeholders had already concluded that increased tax transparency was the solution to demonstrating effective management of tax risk, although to date there has been no consensus on the form and content of, or the audience for, increased tax disclosures. HMRC continues to shape this agenda and organisations are encouraged to ensure they have appropriate plans in place to ready themselves for increased transparency.

We see five key issues to consider when forming a reputational tax risk management strategy:

1. Proactive monitoring of the changing global regulatory landscape
2. Knowledge of what your external tax communications say about your organisation and with changes being made when appropriate
3. Assessment of how ready you are to respond to questions from stakeholders
4. The ability to draw upon your global tax footprint information to ensure a consistent story is given to all your stakeholders
5. Identification of all your stakeholders, remembering these can be internal as well as external

Further information

If you are interested in a meeting to discuss your approach to tax risk, strategy and transparency and our experience of working with organisations in this area, please contact us.

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