Budget Representations 2017
The Correspondence and Enquiry Unit
HM Treasury
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The Institute of Directors is Britain's oldest business representative body, founded in 1903 and awarded a Royal Charter in 1906 obliging us to foster a climate favourable to entrepreneurialism and wealth creation. While the IoD consists of 35,000 members, predominantly the leaders of small- to medium-sized businesses, the below representations reflect our view of what would be most beneficial to the UK business community and economy at large, and therefore the well-being of the country itself.

IoD Recommendations to HM Treasury for Budget 2017

Preamble

Our overarching concern for Budget 2017 – and, indeed, the remaining Budgets in this Parliament – is that the Brexit process does not become an excuse for delaying much-needed and overdue broad-based reform of the UK tax system. It should be noted that the proposals we put forward in this document are proposals for both the March 8h Budget and the Autumn Budget to come.

Real reform to enhance competitiveness is needed from both business and personal taxation perspectives, and the rapidly changing economic drivers which will continue to apply regardless of the outcomes of the pending Brexit negotiations. These developments will naturally require real thought from HM Treasury.

Overall, our key message to Government is that the launch of tax reforms and the simplification process cannot be postponed to 2019 (or beyond) if the tax system is to be aligned with the UK's economic imperatives and with the next election firmly pencilled in for 2020, now is the time to demonstrate real ambition.

The Economic Context

Since the vote to leave the European Union, it is safe to say that confidence has been volatile. However, as we enter 2017, confidence is as high as at any point since June. The following results, from IoD member surveys, give an indication.

How optimistic are you about the prospects for the wider UK economy and for your organisation over the next 12 months?

Net optimism

	July	**September**	**October**	**December**
Economy	-8%	15%	-20%	15%
Organisation	25%	38%	25%	50%

December survey: Comparing the next 12 months with the last 12 months, what do you believe the outlook for your (primary) organisation to be in terms of:[1]

	Revenue	Profitability	Investment	Employment
Much higher	10%	8%	6%	3%
Somewhat higher	50%	38%	25%	27%
No change	25%	35%	50%	53%
Somewhat lower	13%	16%	13%	12%
Much lower	1%	2%	4%	2%
Don't know	1%	1%	1%	2%
Net	+45	+28	+13	+17

It is noticeable however that investment and employment are the weakest areas. The positive net figure for additional investment we saw in December, indeed, was the only positive figure we have seen since June.

This is a promising picture, but one only needs to look at the negativity in October – the month in which we saw sterling crash against both the dollar and the euro – to see how quickly the tide can turn. In short, we are not out of the woods yet.

[1] Figures may not total 100% due to rounding

As such, as we move towards the Budget, it is our view that the Government should be more ambitious than in the previous Autumn Statement, and particularly look at measures to encourage investment and kick-start overdue radical reform of the tax system.

Furthermore, we have been heartened by the indications of what the Government's Industrial Strategy may entail, particularly with regards to an expected focus on skills, infrastructure and research and innovation. While recognising that spending cannot be allowed to spiral out of control, we would urge HM Treasury to work with business groups after the Industrial Strategy is published to ensure that those proposals felt to offer the greatest economic return are given adequate resources to succeed.

Key Themes

We highlight five areas where we consider that tax reforms should be prioritised:-

1. Aligning taxation with the increasingly flexible labour market so that taxation considerations do not take precedence over more important commercial choices.

2. Responding to global (including European) tax competition and developments so that the UK tax system – and tax rates – facilitates the UK re-establishing itself as a second-to-none choice for global entrepreneurs and foreign direct investment.

3. Demonstrating a determination to implement broad-based simplification of the increasingly complex UK taxation system faced by both business and individual taxpayers.

4. Improving the interface between HMRC and business taxpayers so that the ongoing focus in the media upon actual – and alleged – tax avoidance does not damage the UK economy by the perception that tax planning is undesirable or even unacceptable.

5. Recognising that multinational corporations; FTSE350 companies; mid-sized businesses; small companies; and, microbusinesses ought to face (broadly) comparable taxation liabilities but require different focuses and policies to deliver this.

Furthermore, we recognise that this process is also about setting spending priorities. We have spoken already of the need to align Treasury decisions with what we expect to be a cross-cutting Industrial Strategy where appropriate. In particular, we would focus on three main issues.

1. Infrastructure, both physical and digital, must be a priority. This does not, however, mean all-singing, all-dancing, *grand projets.* Rather, our members – and economic theorists – would prefer the focus to be on the upgrading of existing infrastructure and, where new projects are deemed to be of value, small-scale interventions. While not the most exciting, improvements such as lengthening platforms, dualling A-roads where they bottleneck, and improving rolling stock are more easily deliverable, at lower cost, and yet often have a similarly transformative effect. On the digital side, it should remain the Government's ambition to lead the world.

2. The ongoing skills shortage, now reported to us by our members for a number of years, represents one of the most significant challenges to the domestic economy. In member surveys, it is ranked alongside our uncertain trading status with the European Union as a worry for British businesses. Where appropriate, and working with both the Department for Business, Energy and Industrial Strategy and the Department for Education, the Treasury should ensure that significant funding is available for more professional careers advice within schools, for re-training employees in older and

potentially endangered industries, and for the touchpoints of 'lifelong learning' such as night schools, technical schools and further education colleges.

3. In light of our vote to leave the European Union, there is significant uncertainty as to the future of EU-originating funding, with particular concerns around research and innovation finance through programmes such as Horizon 2020. British universities, research parks and other institutions are already feeling a blowback from our vote to leave, as continental partners seek to find alternative partners whilst our uncertain status continues. This cannot necessarily be helped, and is in all likelihood a passing concern. However, research and development will be absolutely crucial to meeting Britain's productivity and agility challenge. We would urge the Treasury to echo the Prime Minister's commitment to science and innovation to ensure that British businesses, working in concert with Government and public institutions such as universities, do not lose out to foreign economies more focussed on future-proofing their businesses.

We have listed below our principal priorities which are responsive to these key themes.

Immediate Policy Changes

- Our members running mid-sized businesses continue to emphasise the importance of the Annual Investment Allowance ('AIA') to incentivise investment in plant and machinery and thereby improve productivity. Regardless of how optimistic one might be about the outcome of Brexit negotiations – and the IoD is more optimistic than others, even if we do accept these are challenging times – there is little question that a knee-jerk response to to uncertainty could be to hit the 'pause' button on significant capital outlay. While businesses are growing used to uncertainty and confidence is increasing, there is always the risk that (as has occurred in previous months) that confidence could decline significantly. The important thing when business confidence is relatively high is to build on it. As such, increasing the AIA cap to, say, £1 million per annum would boost investment, productivity and growth in this key sector of the UK economy and employment opportunities. We are of the strong belief that the relatively minimal cost to the Treasury – indeed, overwhelmingly a timing cost only - would have an outsized effect on business behaviour in the short- to medium-term.

- Our members continue to support the Government's manifesto pledge to deliver the lowest corporation tax rate in the G7, recognising that it is a valuable signpost for a business friendly tax system. If it appears that there will be downward pressure on corporation tax in the United States as a result of the new political leadership in that country, then the United Kingdom should respond by announcing Corporation Tax cuts of 1% to 18% in FY2017, 17% in FY2019 and 15% for FY2020. This would be particularly appealing not just to overseas investors considering capital investment in the United Kingdom, but would be seen as encouragement to medium-sized firms looking to grow.

- We consider that the significant increases in business rates scheduled to be introduced from FY2017 should be re-visited. By this we do not mean that the overarching principle that business rates in aggregate ought to rise by the increase in the CPI – and no more – should be abandoned. But the substantial impact upon small and medium sized business should be **recognised by significantly expanding the business rates reliefs already available to microbusinesses** which occupy business premises with a rateable value of up to £15,000 (and £51,000 for the lower business rates multiplier). As most business rates are paid by much larger corporations, extending business rates relief to all SMEs will not be unduly expensive to the Exchequer in comparison to its broader economic impact including business continuation and expansion and the knock-on effects on employment. This would in particular benefit those microbusinesses looking to expand and grow; precisely the kind of 'scaling' we should be encouraging right across the UK economy. **If we were asked to choose one single measure in the March Budget, it would be alleviating the impact of the business rates increases which affect SMEs occupying business properties with rateable values up to, say, £100,000 rateable value.**

- Furthermore, there are coherent arguments for a fuller review of the business rates system more generally, with modern technology and 'big data' advances in theory making it possible to have a more responsive, 'real-time' ratings system, as opposed to the five- or indeed seven-year cycle of plateaus and damaging cliff-edges.

- The Chancellor should reaffirm that, whilst the UK will implement the outcomes of the OECD/G20 BEPS outcomes, this will be responsive to the scale, timing and compliance approach adopted by other governments so that the UK does not 'gold-plate' the outcomes to the disadvantage of UK businesses, thereby reassuring investors that UK will not become a less desirable location for global entrepreneurs and foreign direct investment by multinational companies.

- Re-assure tax compliant SME businesses that authentic tax planning is permissible and indeed encouraged by instructing HMRC to issue a tax planning 'white-list', thereby encouraging genuine investment decisions and transactions to take place by removing unnecessary/perceived tax risks.

- We remain very supportive of the Government's Making Tax Digital initiative but recommend that due regard is given to the suggestions for a somewhat longer rollout period for microbusinesses and that the proposed penalties are waived for a transitional period for such businesses.

Consultations

We remain supportive of the Government's business tax roadmap for tax reforms excluding necessary remedies to counteract tax abuse and aggressive tax avoidance. Indeed, we consider that that the roadmap should be extended to include all forms of business and personal taxation.

Accordingly, we recommend that the Government announces consultations upon the following key areas for tax reform and simplification, again bearing in mind that considering the political concerns around any radical reform of the tax system these consultations must happen in the near future if they are to be put into effect by the end of the Parliament:-

- The potential advantages of reforming the taxation of SMEs so that they face a simplified tax system in comparison to MNCs and listed companies which, unavoidably, generally have more complex tax issues. The proposed ConDoc should examine areas such as the:-
    - Introduction of a replacement, simplified company tax for SMEs focussed upon verified accounting profits adjusted only by depreciation, capital allowances and AIAs
    - Role for tax transparency for businesses which elect for this to remove the complex interfaces between corporation tax on profits, income tax on remuneration, bonuses and dividends and dividend tax on distributions. Such consultation should not be restricted to Government & tax technical bodies, and should take particular note of the perspectives of businesses, and introducing the possibility of electing for a fixed tax rate upon all forms of payments to owners of SMEs, similar to that of the S-Corps status offered in the United States

- Combining capital gains tax and inheritance tax into a single capital tax which taxes capital gains upon lifetime disposals and gains accruing up to an individual's death whilst preserving the existing major exemptions and reliefs (apart from the CGT exemption for gains arising between acquisition cost and probate value). The objective being to remove arbitrary incidence of both existing taxes and tax - but not double tax - all gains outside key business and personal reliefs and exemptions

- Simplifying, liberalising and democratising EIS/SEIS/VCT reliefs to encourage investment in start-ups and scale-ups including both relaxing the over-engineered and restrictive criteria for these tax reliefs and simplifying the relevant investor protection legislation so that the key over-arching risks are highlighted but this is achieved at a lower compliance cost for such businesses seeking vital external equity capital.

- Launch a Tax Commission to report in Winter 2018 upon the impact of the flexible economy upon tax revenues and ensuring that a 'level playing field' is established between a) the employed & self-employed and b) the established/traditional and new/digital economies. This refers not just to the 'shared economy' and the attached platforms, but to the differences in business rate liabilities between, say, online-only stores and their warehouses in low-land-value areas, versus high street sellers, and so forth.

Longer Term Budget 2017 Reaffirmations

We recognise that there are many tax reforms, simplifications and reductions which the Government would like to introduce but considers it cannot introduce immediately.

Nevertheless, both businesses and individual taxpayers ought to be reassured that 1) such beneficial tax reforms remain on the Government's agenda or that 2) rumoured specific tax increases are *not* in prospect. Specifically, this forthcoming Budget should reaffirm that the Government:-

- Intends to introduce a £12,500 personal allowance and a £50,000 higher rate tax threshold (i.e. a £37,500 basic rate tax band) during this Parliament and ensure that, in future years, these thresholds keep pace with consumer prices / earnings so that fiscal drag does not continue / re-commence.

- Wishes to remove the income tax 'spikes' at £50,000pa and £100,000pa thereby improving incentives to individuals to strive for promotions, re-locate and move to more productive roles.

- Intends to restore the long-term political consensus for a top rate income tax rate of 40% by removing the tax inefficient additional (45%) rate of income tax which, inter alia, discourages bonuses and dividend distributions.

- Confirms that there will be no further restrictions to or reductions in the tax relief for personal pension contributions introduced in the current Parliament to prevent/reduce unnecessary speculation that the Government is planning to withdraw the existing reliefs available.

- Confirm the commitment to ensure that no other G20 country has a lower corporation tax rate than the UK.

- Confirm that local authorities will only be permitted to increase business rates for infrastructure improvements after having obtained the support of the local business community (e.g. through the existing LEPs).

The IoD remain keen to discuss further. Please do use the below contact details.

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