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Exploring complex businesses' tax processes and readiness for Making Tax Digital

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Glossary of terms

Term	Definition
CCM	**Customer Compliance Manager:** All large business customers have an allocated HMRC CCM who works with the business to ensure they are tax compliant.
CIS	**Construction Industry Scheme:** Contractors deduct money from a subcontractor's payments and pass it to HM Revenue and Customs (HMRC).
CT	**Corporation Tax:** A tax on the taxable profits of limited companies and some organisations including clubs, societies, associations, co-operatives, charities and other unincorporated bodies.
ERP	**Enterprise Resource Planning:** Business process management software that allows a business to use a system of integrated applications to manage the business and automate many back-office functions related to technology, services and human resources.
FSSC	**Financial Shared Service Centre:** A central support function within an organisation which carries out financial and administrative services for parts of the company.
Government Gateway	The **Government Gateway** is an IT system used to register for online services provided by the UK Government.
ITSA	**Income Tax Self-Assessment:** Self-Assessment is a system HMRC uses to collect Income Tax. Tax is usually deducted automatically from wages, pensions and savings. People and businesses with other income must report it in a tax return.
Large businesses	For the purposes of this research, large businesses are the largest and most complex businesses in the UK, which have been allocated a CCM (Customer Compliance Manager) within HMRC's Large Business Directorate.
LLP	**Limited Liability Partnership:** This is a form of incorporated business structure that is similar to a limited company. An LLP is taxed like a partnership, with tax returns being filed for the LLP and for each member, and each member being taxed on his or her share of the profits.
Mid-size businesses	HMRC defines mid-size businesses as those with Corporation Tax or Income Tax Self-Assessment turnover above £10 million; and/or more than 20 employees. There are additional criteria assessing a business's complexity which also qualify a business as mid-size, for example, if it has more than 10 partners.
Manual	In this study, the term manual refers to processes that are not automated. These process are likely to include an employee reviewing data records stored in a spreadsheet or another form of digital technology.

MTD	**Making Tax Digital:** Making Tax Digital aims to transform the tax system for businesses, including companies, sole traders, self-employed people, partnerships and property landlords by requiring customers to keep digital records through software or apps and update HMRC with summary tax information on a quarterly basis. The aim of MTD is to make tax administration more effective, more efficient and easier for taxpayers to see what they owe, reduce mistakes and save time spent trying to resolve problems.
NI	**National Insurance:** National Insurance contributions are paid to qualify for certain benefits and the State Pension.
Partnership	In a partnership, partners personally share responsibility for their business. This includes any loss the business makes, and any bills for things that are bought for the business such as stock or equipment. Partners share the business's profits and each partner pays tax on their share.
PAYE	**Pay As You Earn:** Employers normally have to operate PAYE as part of payroll. PAYE is HMRC's system to collect Income Tax and National Insurance from employment.
RTI	**Real Time Information:** Under RTI, information about tax and other deductions under the PAYE system is transmitted to HMRC by the employer every time an employee is paid.
VAT	**Value Added Tax.** The tax paid on most goods and services.

Executive summary

Making Tax Digital is a key part of the government's plans to become one of the most digitally advanced tax administrations in the world, modernising the tax system to make it more effective, more efficient and easier for customers to comply with. Under Making Tax Digital (MTD), businesses will keep digital records and use compatible software to update HMRC.

The aims of the research were to explore the management and reporting of tax information and general awareness of MTD with complex businesses. HMRC anticipate that in the context of MTD, complex businesses will include large[1] and mid-size[2] companies and partnerships. The research agencies Kantar Public and IFF conducted a total of 42 interviews with mid-size and large businesses for this research. Fieldwork was conducted between 10th March and 13th April 2017.

Key findings

- Businesses reported using a number of different systems and software to manage their tax affairs. This often included using customised[3] and off-the-shelf software, as well as the use of spreadsheets. Manual[4] processing was also a pivotal part of managing tax affairs as most businesses reported that at least some part of their processes required manual input, which tended to be the most burdensome.
- Mid-size businesses reported higher use of external agents, and this was predominantly for managing Corporation Tax (CT) and Income Tax Self-Assessment (ITSA). Large businesses generally tended to undertake their tax affairs in-house with a few businesses using an external agent for CT.
- Generally, businesses felt they had the systems and staff in place to successfully manage their current tax reporting processes, although they recognised inefficiencies in their current processes.
- Businesses were generally supportive of the concept of digital change and the shift towards interacting more digitally with HMRC.
- Businesses were generally satisfied with their relationship with HMRC. However mid-size businesses reported negative experiences with HMRC helplines. Both

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[1] For the purposes of this research, large businesses are the largest and most complex businesses in the UK, which have been allocated a CCM (Customer Compliance Manager) within HMRC's Large Business Directorate.
[2] HMRC defines mid-size businesses as those with Corporation Tax or Income Tax Self-Assessment turnover above £10 million; and/or more than 20 employees. There are additional criteria assessing a business's complexity which also qualify a business as mid-size, for example, if it has more than 10 partners.
[3] Software which had been adapted and programmed to meet the wider needs of the business (not just the tax department).
[4] In this study, the term manual refers to processes that are not automated. These process are likely to include an employee reviewing data records stored in a spreadsheet or another form of digital technology.

large and mid-size businesses suggested improvements could be made to the Government Gateway to make it more interactive for customers.

- Awareness of MTD varied considerably. However, businesses were in general unclear of the details of MTD, and there was a desire for more information. As businesses felt they did not have sufficient information about MTD, they were unable to give fully-informed details about how it would impact their current processes and systems.

- Some businesses thought MTD could result in quicker and easier processes for dealing with their tax affairs, by reducing paperwork and providing a more holistic view of tax processes. Some concerns raised around MTD were about quarterly reporting, what ‘real time’ means in practice, software incompatibility, and increased resource and costs resulting from MTD.

- In terms of support needs to make the transition to MTD, businesses reported that HMRC should provide more detail on the MTD requirements, allow a transition period for adapting to the new changes and work collaboratively with them to understand how MTD should be implemented in complex businesses.

Conclusion

Across all business sizes, there is a mix of manual and digital tax processing being undertaken. There is evidence that businesses are transferring data across multiple systems and software and that detailed checks are carried out internally and externally by finance and tax professionals before the information is submitted to HMRC. Businesses are able to produce the information required by HMRC on time although many are aware that they are making do with less than efficient systems and processes.

Currently, there is low awareness of MTD among complex businesses however businesses were broadly supportive of the principle of increasing their digital interaction with HMRC. They also described broadly positive experiences of using digital processes to file reports and submit payments. However, they struggled to relate these positive views to MTD, or indeed any future changes to managing their tax affairs, primarily due to concerns that changes would exacerbate current inefficiencies in how they manage their tax affairs. This limited their ability to visualise any future benefits.

1. Introduction

1.1. Background

The MTD reforms are a key part of the government's initiative to transform HMRC into a digital tax authority, and aim to make it easier and quicker for individuals and businesses to keep on top of their tax affairs.

MTD will require businesses to keep digital records through software and update HMRC with summary tax information on a quarterly basis. As an initiative to reduce the tax gap, MTD will help reduce error and failure to take reasonable care which accounts for £9.4bn of tax lost annually. In helping businesses get their tax obligations right first time, MTD will also provide more certainty and a clearer view of their tax position.

At Budget 2015, the government set out its vision for MTD stating that it will affect businesses, self-employed people and landlords.

At the time of this research (10th March to 13th April 2017), HMRC's plan was for customers to start using the new digital service from:

- April 2018 for Income Tax and National Insurance contributions (NICs)
- April 2019 for VAT; and
- April 2020 for Corporation Tax (CT).

However, since this research was completed the government announced that only businesses with a turnover above the VAT threshold (currently £85,000 per annum) will be required to start using the new MTD system from April 2019 and only in respect of their VAT obligations. Smaller businesses with a turnover below the VAT threshold will not be mandated to use the new system, but can do so voluntarily. Businesses will not need to use the new MTD system for other taxes until at least 2020 but can choose to do so.

1.2. Research Objectives

The aims of the research were to provide a deeper understanding of the following:

- Current levels of awareness and understanding of MTD among relatively complex businesses;
- How businesses currently manage and report on their tax affairs and their views and experiences of this process;
- Views about how businesses would like to interact with HMRC in a digital age.

HMRC anticipate that in the context of MTD, complex businesses will include large and mid-size companies, and partnerships. Complex business will also have some of the following characteristics:

- one parent company and multiple subsidiary companies;
- complex VAT and/or CT group arrangements;
- business complexity driven by the volume of transactions that they have with HMRC.

1.3. Methodology

The research agencies Kantar Public and IFF conducted a total of 42 interviews with mid-size and large businesses for this research. HMRC's operational definition of a mid-size business is one that has annual turnover above £10 million and/or 20 or more employees[5]. For the purposes of this research, large businesses are the largest and most complex businesses in the UK, which have been allocated a CCM (Customer Compliance Manager)[6] within HMRC's Large Business Directorate. Typically, these businesses have a turnover of more than £200m, but other factors are taken into account when determining a business's complexity[7].

Kantar Public conducted in depth face-to-face and telephone interviews with a total of 48 strategic and operational staff working in the finance departments of 30 mid-size businesses. IFF conducted 12 face-to-face case studies with 40 individuals from large complex businesses. Fieldwork was conducted between 10th March and 13th April 2017.

All businesses were recruited from a sample of Tax Managers and Financial/Tax Directors that had taken part in the Large Business Survey 2016 and Mid-size Business Survey 2016 (for more information on the Large and Mid-size Business surveys, please see the links below). Businesses participating in this research had agreed to be re-contacted for the purposes of future qualitative research. All participants were responsible for one or more of the following tax obligations: Corporation Tax (CT); Value Added Tax (VAT); or Income Tax (IT) in terms of preparing and/or reviewing tax returns.

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[5] https://www.gov.uk/government/publications/mid-size-business-customer-survey-2015
[6] Previously known as Customer Relationship Manager (CRM). All large business customers have a an allocated HMRC Customer Compliance Manager (CCM) who works with the business to ensure they are tax compliant.
[7] https://www.gov.uk/government/publications/large-business-survey-2015

1.4. Profile of businesses that participated in the research

Participants were purposively selected (using a screening questionnaire) to achieve agreed quotas and ensure a wide range of complex businesses participated in terms of size, ownership structure, group status and sector. As a result, the overall findings in this report are not representative of the mid-size and large business population.

Table 1. Profile of mid-size businesses participating

Criteria	Description	Number completed
Turnover	Under 10m	11
	10-50m	12
	50-100m / 100-449	7
Number of employees	Less than 20	1
	20-49	9
	50-99	3
	100-249	6
	250+	11
Company Structure	Group owner	5
	Singleton	14
	Owner sub	1
Ownership	Subsidiary	10
Partnership	Foreign Owned	7
	Partnership	6
Total mid-size business		**30**

Table 2. Profile of large businesses participating

Criteria	Description	Number completed
Turnover	£50-100m	2
	£100-499m	5
	£500m+	5
Number of employees	Less than 500	5
	More than 500	7
Group Structure	Part of larger foreign owned group	5
	Part of a larger UK owned group	3
	Not part of a larger group	4
Sector	Oil and Gas	1
	Finance	2
	Other sectors	9
Legal status	Partnership/Limited Liability Partnership (LLP)	2
	Other legal structure	10
Total large business		**12**

2. Overview of complex businesses’ management of tax

During the interviews, businesses were asked to describe the processes involved for three core tax obligations: VAT, CT and IT. In addition to these core taxes, businesses also mentioned the tax process in relation to other obligations relevant to their industry sector including Construction Industry Scheme (CIS), Beer Duty, and Machine Games Duty.

This chapter provides a summary of the processes involved across all tax liabilities; further chapters will explore each individual tax obligation in turn.

2.1. Who is involved in the process?

Across complex businesses participating in the research, there was a mix of internal and external support on tax management and processing. The number of people involved in the tax processes within businesses varied according to the size of the business. At the smaller end of mid-size businesses[8], there may only be a single person often completing VAT returns and outsourcing CT calculations to an agent. In larger mid-size businesses, there could be a multi-layered management structure with several teams handling the different aspects of the financial and tax reporting.

For large businesses, the processing (collating information) and reporting of each tax obligation for each company was at a minimum led by two people – i.e. the person with overall responsibility for VAT (most often the VAT Manager/Head of VAT/Indirect Tax Manager) and the person with overall responsibility for CT (most often the Head of Tax/Tax Director, or in some cases a specific CT Manager). Among the Limited Liability Partnerships (LLPs) those with overall responsibility for IT were the Partner Tax Manager/Head of Partner Tax. In some instances, the team and number of people involved in the processes was much larger, particularly where the business had a number of overseas operations and different tax departments across the world.

Mid-size businesses tended to use agents to calculate and submit their CT returns with the business providing the requisite information from their accounting systems e.g. providing an ‘audit pack’ or a draft CT calculation. For IT, most partnerships handled these processes internally. Mid-size businesses generally tended not to use agents for the VAT process, and managed this in-house, but there were some instances whereby

[8] Here, the ‘smaller end’ of the mid-size businesses refers to businesses with under 10m turnover (20 or more employees); the ‘larger end’ refers to businesses with over 50m turnover; however these are rough guidelines rather than clear cut definitions.

the processing and submission of the VAT return was subcontracted to a self-employed bookkeeper or accountant (agent).

In comparison, large businesses tended to manage their tax processes in-house but two of the businesses in this research used agents for further support. This was mainly for outsourcing to check VAT and extra computations on CT returns as well as for part of the compliance process for both VAT and CT. Agents were primarily used due to resourcing issues within the businesses.

In addition to tax agents, there were some cases where large businesses used Financial Shared Service Centres based abroad to collate data from individual companies within a group, this service reviewed the data before consolidating it into one return for HMRC.

2.2. Use of digital methods for reporting

The processes that businesses, of all sizes, used for meeting their tax obligations were not entirely digital. Most businesses stated that at least some part of their processes required manual input (e.g. manually inputting figures) which tended to be the most burdensome aspect.

Generally, businesses used a wide variety of customised and off-the-shelf systems and software to manage their business. Some of the larger businesses used Enterprise Resource Planning (ERP) solutions which act as a central repository of business information and had been programmed and adapted to meet the wider needs of the businesses.

Most of the software used by mid-size businesses was off-the-shelf, but some had been customised by the software supplier to better meet the business' needs. Large businesses tended to use customised[9] software, this is software which had been adapted and programmed to meet the wider needs of the business (not just the tax department).The two large partnerships participating in the research tended to use bespoke software (i.e. software that they built themselves) and this tended to be due to the perception that IT is complicated and there is not availability of relevant software which meets the business needs. More standard accounting and reporting software was used to assist in the reporting and checking of tax data drawn from the ERP solutions. Businesses used software that met their various needs[10]. For example:

- Integrated stock control and accounting;
- Project Analysis;

[9] Software which had been adapted and programmed to meet the wider needs of the business (not just the tax department).

[10] This is how the businesses referred to the software they used. It is possible that the software has many other functions; businesses either did not refer to them or did not use them.

- Customer sign-up and cash sales;
- Accounting, including sales and purchase ledgers and VAT; and payroll with additional modules;
- Production of tax returns and statutory accounts;
- Payroll; and
- Estate management and accounting.

Businesses also tended to use spreadsheets for preparing information for the reporting of VAT, CT and IT. This was predominantly for formatting/inputting data, checking data for accuracy and making adjustments for exemptions, partial exemptions and reliefs such as fuel scale charges.

Reasons for using particular software were often historic and pre-dated the participants' time with the company. In many cases, businesses (mid-size and large) stated that the systems in place were often historic/legacy systems (i.e. businesses acquired new businesses and adapted rather than overhauled their existing processes). In a few instances, the systems were a requirement of a parent company, in some cases a foreign owner required all group companies to use the same accounting software. In some instances, a change of software occurred when a new financial director/manager joined the organisation. This was either because existing software was becoming too difficult and expensive to maintain and update or because the company had decided to overhaul their systems and integrate a wider set of functions such as stock control and accounting.

The software was not always chosen or designed by the team responsible for processing the tax. Some of the reasons for using particular software were because it was deemed the best type of software available to deal with a particular type of tax or because it was a good fit for a particular business function.

One large business explained that, in some cases, different pieces of software were used by different individual businesses because they were more suited to their function. For example, they mentioned that a type of ERP[11] software is used by one part of their business because it is better for tracking high-volumes of stock, whereas another part of their business used a different type of software designed for manufacturing companies because it was better suited to the packaging of this stock. On the other hand, this business stated that different software packages within their group do not *"always talk to each other"* simply because that is how their business had "*evolved over time*". They described cases where they have acquired new businesses which have brought in their

[11] This was a type of Enterprise Resource Planning (ERP) software package which is used to control the operations of manufacturing companies.

own existing systems and adapted them to their group reporting requirements (as opposed to changing them completely).

In several cases, businesses were exploring the feasibility of making changes and investing in new digital processes to assist with reporting based on the data drawn from their ERP solution. One business had recently introduced software to assist with CT iXBRL tagging[12]. However, this was not felt to be working smoothly as it is an "off-the-shelf" accounts tool rather than a specific tax tool geared towards the needs of the business.

Some of the pinch points businesses reported experiencing with their software arrangements were as follows:

- Business processes not being fully software integrated. This might be the use of separate systems for accounting and payroll or stock control and accounting and taxes such as Beer Duty and Machine Games Tax being collected separately to the accounting system (but *"Journaled in"*) and submitted to HMRC on paper forms.
- A few businesses used accounting software designed outside the UK to meet the needs – tax or otherwise – of the 'host' country. This software did not produce VAT outputs in the form required in the UK. Businesses reported having to spend time manually inputting figures, given that automation was not possible.
- With very limited exceptions, the VAT report produced by accounting software is not directly submitted to HMRC but is subject to adjustment for exemptions, partial exemptions and reliefs such as fuel scale charges. Participants indicated that they transfer the information from their accounting software or their spreadsheet manually into HMRC's VAT portal.
- The accounting software was said to be unable to produce a final CT report. While the information that is used in the CT computation is extracted from the accounting software, the software is not able to deal with the various allowances and reliefs.

Over time, businesses had honed their processes so that they would be able to meet the required internal and external reporting deadlines and produce the correct information for accounting and tax purposes. Nevertheless, businesses did sometimes feel that their systems could be more efficient, in the sense that they often involved a lot of manual checking/manipulation of data, but suggested that they were willing to cope with this

[12] XBRL or iXBRl (eXtensible Business Reporting Language) is a process that adds computer-readable tags to business data. It allows the data to be processed automatically by software. The tags are included in the business accounts and computations that are sent to HMRC as part of the Corporation Tax return. For more information see: https://www.gov.uk/government/publications/xbrl-guide-for-uk-businesses/xbrl-guide-for-uk-businesses

given that they are effective, in the sense that they allow them to accurately report tax information.

> *"If it's not broken, why invest time and money fixing it? We've got quite a high standard of output. The accuracy level is quite high. The number of errors that we disclose is low because of that high standard of scrutiny."*
>
> ***Part of a larger foreign group, 1000-4999 employees, Real Estate***

> *"The first critical point is making sure that the data in the pack ties back to the financial statements we're preparing and submitting. Second critical point is making sure that the mapping of all of those, both revenue and expenses, and capital spend is correctly mapped so that the calculations can work correctly. The next critical point is for the auditors to review that and have comfort that what they are bringing out into the tax return is correct. The next critical point is for me to review those tax returns based on the information to hand and review. We then go from, and then the next step is to check the iXBRL tagging of the stats."*
>
> ***Limited company, £10-30m turnover, 250+ employees, Retail***

2.3. Perceptions of complexity

HMRC anticipate that in the context of MTD, complex businesses will include large and mid-size incorporated companies and partnerships which also have some of the following characteristics:

- one parent company and multiple subsidiaries;
- complex VAT and CT group arrangements;
- or complex VAT or CT group arrangements;
- business complexity driven by the volume of transactions that they have with HMRC.

When asked to define the nature of a complex business, businesses considered the following key areas:

- The business structure;
- Operational environment/specialisms of the business;
- The approach to business trading;
- International elements; and,
- Specific technical tax issues.

The table below provides key areas raised by complex business:

Table 3. Features of complexity

Overarching theme	Feature of complexity
Business structure	Multi-company structure with many subsidiaries
	Joint ventures (i.e. business arrangements in which two or more parties agree to work together)
	Mixed entities (e.g. corporates and partnerships)
	Ownership by a Trust
Operational environment/specialisms of the business	Seasonal trading
	Managing a bonded warehouse
The approach to business trading	Inter-company trading
	Uses regulated client accounts that are kept separate for overall business accounts (e.g. legal practices)
International elements	International trading – importing and exporting
	Multi-currency trading
	Numerous income streams from UK-based and internationally owned businesses
	Cross-charging between businesses that may be UK or internationally based
	Using complex ways to shelter profits off-shore (i.e. tax havens)
Specific technical tax issues	Dealing with multiple taxes e.g. VAT, CT, PAYE, NI, IT, CIS, Beer Duty etc.
	Dealing with products that have different VAT rates

Overarching theme	Feature of complexity
	Employing people who are self employed
	Large number of tax exemptions, allowances and reliefs

Despite many of the features described above applying to businesses in the research, the majority of mid-size businesses did not see themselves as complex. For large businesses the perception of complexity was mixed. Some large businesses did not perceive themselves to be very complex, while others felt they were very complex. For businesses that didn't perceive themselves as complex, this was primarily because while there may be some perceived complexity around the calculation of their tax liabilities – especially CT – participants focussed on the nature of their accounting processes that they had in place and which they considered were straightforward and worked well.

"The processes that run are straightforward."

Part of a family-owned group of companies, £3m turnover, 20-49 employees, Manufacturer

Where businesses identified themselves as complex, they tended to do so because they took into account their structure, trading arrangements, or the computation of their tax liability. Complexity was predominantly associated with characteristics including being foreign owned/foreign trading, different types of ownership (joint ventures, Associate company), mix of entities e.g. Partnerships, corporates etc. which require entities to be brought together into one 'profit pool' to be allocated to individual partners, and group structures.

"I'd say we were a simple business but the complexity comes because we are an international trader – that aspect requires more knowledge within our staff to determine the correct transactional price."

Part of larger UK group, 1000-4999 employees, Manufacturing

"To be fair, I guess we are more complex than simple. The fact that we have an interaction between two companies and the fact that we are partly exempt automatically puts us into a completely different level than your average VAT return…in our case we have a lot of cross charges and a lot of interaction [between companies] and a lot of argument [with HMRC] about the value of the partial exemptions."

Retail, part of a group with a foreign subsidiary, turnover £65m, 250+ employees

3. Managing and processing tax

3.1 Managing VAT

All mid-size and large businesses taking part in this research provided information on their processes for managing VAT. These businesses used a number of different approaches to manage their tax processes. As mentioned above, VAT was predominantly a process undertaken in-house often by the VAT manager/Head of VAT with supporting staff. The number of people involved in VAT processes in mid-size businesses depended on the size of the business, in large businesses there were generally teams allocated to VAT. There were some instances for mid-size businesses whereby the processing and submission of the VAT return was subcontracted to a self-employed bookkeeper or accountant (agent). Large businesses also used external agents for checking VAT returns.

Businesses used a combination of methods to manage their VAT processes, including digital methods such as accounting software and spreadsheets as well as manual processing[13].

The VAT process was generally as follows:

- On either a monthly or a quarterly basis, the business will download all the transactions for the previous VAT period from their accounting software. In most cases, the individual responsible for VAT will manually check each item to ensure that it is correct in terms of whether the items are VAT exempt, zero-rated and has the correct VAT rate applied. Businesses with EU sales will rate the relevant items accordingly. The manual check will also ensure that every transaction has an accompanying invoice or receipt.
- Some large businesses reported that individual businesses feed sales and purchase information into the Financial Shared Service Centre (FSSC) which then downloads the data from the ERP software and prepares VAT returns for each company within the group.
- Once the business is satisfied that all the transactions are correct, the information is loaded into a spreadsheet where adjustments are made for items such as fuel scale charges.
- The output from the spreadsheet was either in tabular form or a template designed to look like HMRC's VAT portal. Many businesses entered the VAT figures manually into the VAT portal. The VAT is then paid by BACs transfer, Direct Debit or in some cases by cheque. Some businesses paid VAT monthly; others paid VAT quarterly.

[13] In this study, the term manual refers to processes that are not automated. These process are likely to include an employee reviewing data records stored in a spreadsheet or another form of digital technology.

- Within the sample of businesses there were some that were net VAT recoverers.

For most businesses, the VAT process was seen as straightforward, albeit potentially time-consuming, particularly when ‘chasing’ receipts from staff for VAT purposes. This was especially so where businesses had many transactions and the company policy was to check that every transaction had the correct VAT rate.

> *"In terms of HMRC it is mainly a straightforward process to support that and have the supporting documents should anything happen and require more info we can easily access that information."*

Under £10m turnover, 250+ employees, mid-size business, Sports club

Some large businesses mentioned that the introduction of the Financial Shared Service Centre (FSSC)[14] had made the process easier by taking most of the burden away and allowing the VAT manager to act more in an advisory role and concentrate on any particular complex issues. However, VAT was not considered to be a simple tax to deal with. Whether supplies were subject to VAT, whether they were zero-rated or attracted a different level of VAT and cross-charging VAT between inter-linked companies all added to the complexity of managing the businesses’ VAT liability.

Overall, most businesses identified no pinch points, however, some businesses identified a few issues with the system. Most businesses considered that they had the systems and staffing in place to successfully manage the VAT reporting process. Where pinch points were identified, these were of the following kind:

- Delays in completing the VAT calculations whilst chasing missing invoices or expense receipts.
- Manual entering of data, adjustments and checking data. For example, one business mentioned that VAT cannot be claimed on company cars where they have been used for private use. Consequently, every month, the VAT team compare the logs for each company car and identify the proportion of fuel on which VAT can be reclaimed – this was described as a manual operation that can be time-consuming.

> *“Not everything is fully automated. We still need this manual intervention to actually match our operational tax flows with what we declare to HMRC.”*

Foreign private equity owned, £33m turnover, 100-249 employees, Mid-size business, Manufacturer

[14] A central support function within an organisation which carries out financial and administrative services for parts of the company.

"The reason it is a manual process is because we are not a straightforward organisation and that's because we have parts of our business that are not full VAT-able, so they're exempt, and once you have those then you're into a manual calculation. I don't think there is a package out there that will solve our kind of problem. I think it's actually quite difficult to look at a software-led solution and we're likely to always be in this rather difficult area of having to manually solve via a manual calculation on an Excel spreadsheet what is our tax liability for that particular quarter."

Part of a larger foreign group, 100-249 employees, Finance

- Dealing with the VAT from multiple companies within the group, each of which may have a different VAT return deadline.
- Having an international dimension to business was particularly complex because it means that the business must adhere to additional VAT rules and regulations.
- Ownership structure – Businesses' processes of reporting VAT adds additional level of group reporting which requires an additional layer of checking.

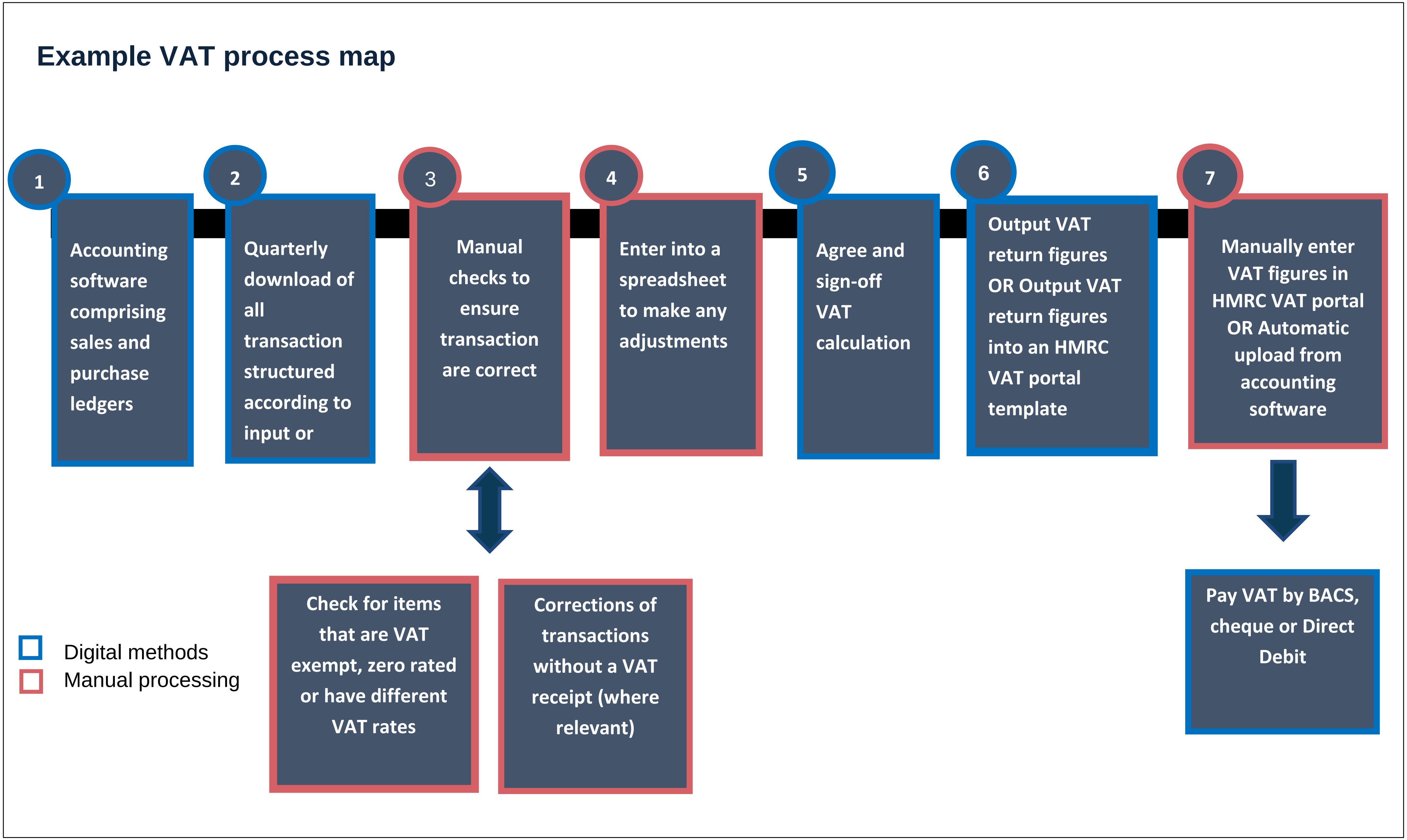
- Volume of transactions - High volume of transactions means more time spent in terms of manually entering and checking data, exacerbating the administrative burden.

"Volume is the biggest challenge, things that are relatively easy for a small number of transactions become challenging when you replicate that over a large number – particularly when you get exceptions to the rules / one-off cases."

Not part of a larger group, 5000+ employees, Oil and Gas

Figure 1 shows an example VAT process map. The process map demonstrates that the general VAT process involves automatic processing at the beginning, with sales and purchase information being fed into the accounting software. There is also manual checking of the transactions to ensure they are correct, before the VAT calculation is agreed and signed off. The VAT figures are then either automatically uploaded into the HMRC VAT portal through the accounting software or the figures are manually entered.

Figure 1. VAT process map example



3.2. Managing Corporation Tax (CT)

Most businesses participating in this research provided information on CT. As mentioned above, mid-size businesses tended to use agents for CT whereas large businesses generally tended to produce CT computations in-house, which was usually the responsibility of the Head of Tax. A few large businesses did report using external agents for some elements of their CT processes such as extra computations of the CT returns as well as parts of the compliance process such as the auditing process.

Businesses in this research followed a mix of approaches, with some paying CT quarterly on account[15], others on an annual basis. Quarterly payers would undertake a quarterly assessment of their profit, often using the previous year as a guide.

The general steps for the CT process were as follows:

- At the accounting period end, the businesses would either undertake an initial assessment of their annual trading profit and prepare a draft CT computation themselves or would pass the required information to the agent to undertake the draft CT computations. Most of the large businesses, but few of the mid-size businesses, undertook a draft CT calculation themselves. Mid-size businesses tended to rely on their agent and would pass an 'audit pack' to their agent. Individual businesses within large businesses would instead complete their 'tax pack' in-house.
- For mid-size businesses, the agent would then review the audit pack and consider what were acceptable allowances and reliefs for the business to include, whereas large businesses tended to do this in-house. Typically, these might be the Annual Investment Allowance, Research & Development (R&D) Tax Credits, Patent Box, other capital allowances and Depreciation. At this point, there would usually be a period when the agent would ask for further information or engage in discussion with the business about whether certain allowances and reliefs would be acceptable to HMRC. This process could take between one and three months.
- Once the computation had been agreed in principle, it was usually reviewed and signed off at Board level – in some cases the Board of the parent company. Thereafter, the business or agent would submit the Company Tax Return electronically with payment being made to HMRC. While payment was due nine months after submission, some businesses made the payment sooner, but most waited until the payment was due.

[15] Generally 'large' companies must pay their Corporation Tax electronically by instalments. A large company is one whose profits for the accounting period in question are at an annual rate of more than the 'upper limit' - currently £1.5 million - in force at the end of that period. There are some exceptions. For details see: https://www.gov.uk/guidance/corporation-tax-paying-in-instalments#who-has-to-pay-corporation-tax-in-instalments

Both the example process maps for mid-size businesses (Figure 3) and large businesses (Figure 4) show the process of reporting CT over a 12 month period. Both mid-size and large businesses in the example use external agents to assist with the CT process. For large businesses, each individual company produces its own statutory accounts which are audited by external agents before being sent onto the Financial Shared Service Centre. The remainder of the CT process in large businesses is then predominantly done in-house. For mid-size businesses, external agents were heavily used for CT returns.

Figure 2. CT process map example for mid-size businesses over a 12 month period

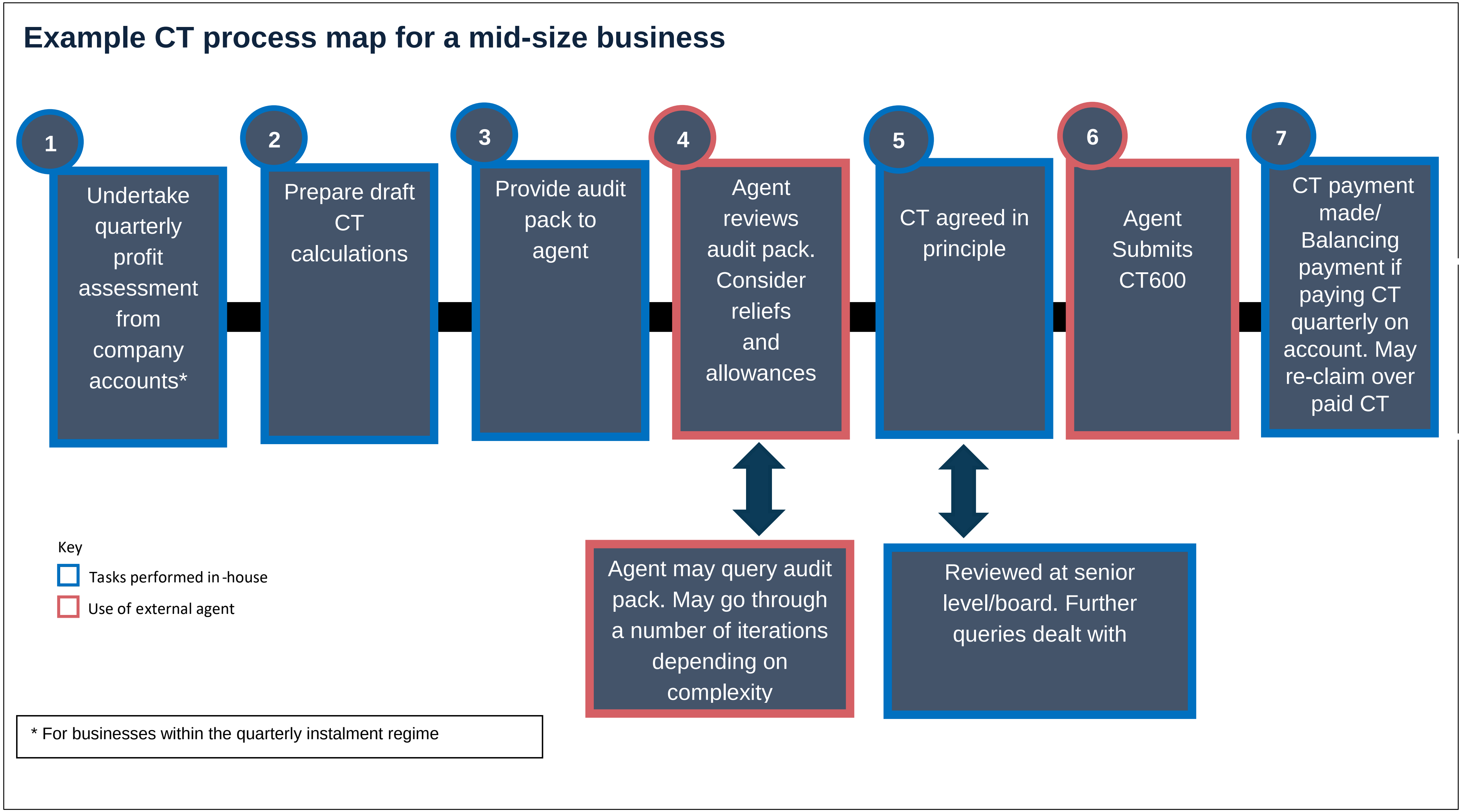
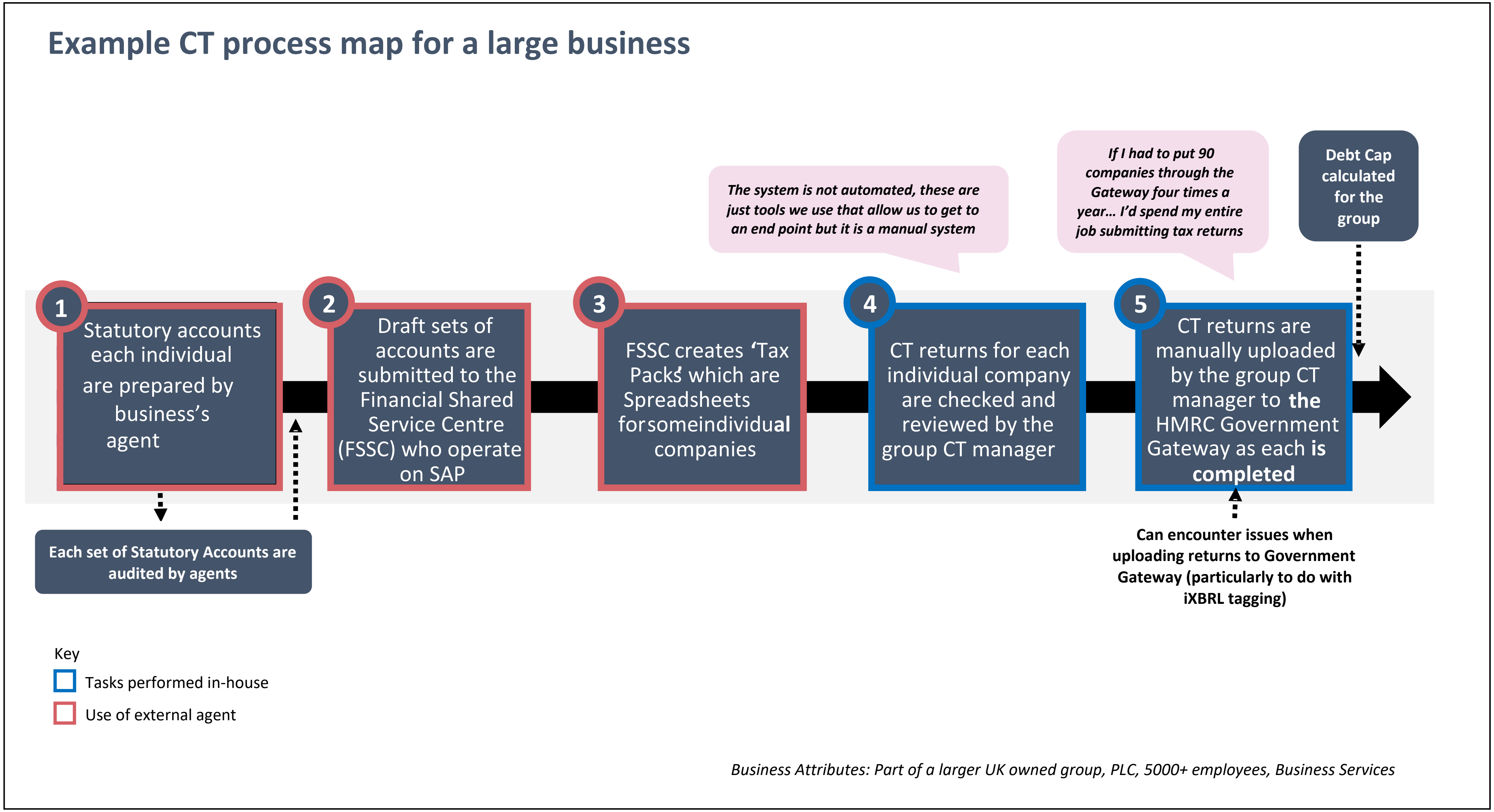


Figure 3. CT process map example for a large businesses over a 12 month period



It was clear when discussing the preparation of the Company Tax return that few mid-size businesses believed they had the internal expertise or software available to feel confident in undertaking the computation themselves. There were a couple of businesses where the Finance Director could undertake the computations themselves using spreadsheets as the business was considered relatively simple from a CT point of view. Nevertheless, for all mid-size businesses in the research, the final computation was undertaken by external accountants, sometimes in association with a specialist tax accountant.

CT was generally considered to be a complex tax to calculate, especially where the business used a large number of allowances and reliefs. This is primarily why mid-size businesses tended to outsource to accountants and tax specialists.

> *"The complexity, such as it is, comes from Patent Box and R&D (Research & Development)."*
>
> ***under £10m turnover, 20-49 employees, Bioscience*** [16]

However mid-size businesses reported the process of providing the requisite information to the agent, whilst time consuming, was not particularly burdensome. As this was usually a significant annual event, businesses had a structured process in place to prepare for this. Nevertheless, there were seen to be some inefficiencies and duplication of effort as often the same information was required for both CT and VAT.

Where problems arose with either the calculation of CT or deciding whether the business was eligible for reliefs or allowances, mid-size businesses considered that HMRC was 'less than helpful'. Typically, mid-size businesses felt that HMRC were not particularly good at making decisions and would simply refer businesses to the HMRC website, which is often where they had started their search for clarity. Similarly, HMRC call centre advisers were generally seen as unable to answer technical questions for CT and businesses consistently complained about the difficulties in getting through to a call centre adviser.

As large businesses tended to manage CT processes in-house, the complexities mentioned were different. All large businesses reported two main complexities of CT, one being about iXBRL tagging which was often a manual part of the CT process adding to the admin burden of compliance.

For example, a large business stated that in-house iXBRL tagging sometimes lead to tagging errors, which meant CT files were rejected by HMRC when the business tried to submit them. This business stated this was particularly problematic in the context of their business because they need to submit returns for multiple businesses.

[16] The Patent Box enables companies to apply a lower rate of Corporation Tax to profits earned after 1 April 2013 from its patented inventions. Businesses can also claim for Research & Development tax relief.

While there was evidence from the interviews that some businesses had sought third party support to assist with iXBRL tagging or had invested in new solutions, many explained they expect it to continue to be a manual process.

The second complexity was the need to conduct manual reviews/checks of the data. Businesses reported that they manually check data for CT returns and they expect that they will continue to do so. This often related to collating and analysing data from individual businesses (when part of a larger group). Some businesses did not have software in place to easily collect data from all of the individual businesses within their group and relied on physically having to locate hard records. For other businesses, they had the software in place to automate the process of collecting data from all of the individual businesses within their group. Although for these businesses, this was still a digital process, it often involved manipulation of data and transferring data from one software solution to another. In the quote below the business explained this also involved hard copy administration:

> *"The main challenge for us is just getting the underlying data used for the returns. That's the most difficult aspect and it's not digital but that's where our time is spent. For example, we can have issues finding hard records – as the head office of the group we may call a site and request to view a hard copy of an invoice on a particular day but the sites can have difficulties locating them."*
>
> ***Part of larger UK group, 1000-4999 employees, Manufacturing***

One large business explained that their accounts team manually enter descriptions from invoices into the software. The finance team then use the software to compile data from a number of sources. Statutory results from each company are then reconciled manually to Statutory accounts and are consolidated/adjusted as necessary by the Head of Tax.

- The statutory accounts from each company are then reconciled manually in a spreadsheet by the Head of Tax and reviewed before numbers are copied from the final report to the HMRC online form. Specific tasks conducted in spreadsheets in relation to the CT process included: external accountants calculate capital allowances and provide reports directly to the team – which are then entered manually into software;
- Manually adjust/correct data as necessary (which usually takes around 2-3 weeks and is undertaken by a junior member of the finance team);
- Analyse all overhead costs (client entertaining, director's costs and salary allocated as stewardship costs for head office or allocated to the rest of the business).

3.3. Managing Income Tax (IT)

Eight of the businesses in the research were partnerships. Each partnership was required to complete a Partnership Return with every partner completing a Self-Assessment Tax Return. Most of the partnerships handled these processes internally; one out-sourced the entire process to their agent, providing the agent with full access to their accounting system from which the relevant information was drawn. In the case of the other partnerships the usual process was for the finance manager/director to complete the Partnership Return based on the information held in their accounting system. This is then agreed by the partners and submitted to HMRC.

The general process was as follows:

Financial data is downloaded from the ERP software to create financial statements. Manual checks/adjustments are then completed to ensure that the data is correct and the data is converted to software to prepare the partnership return.

- Each partner is allocated a profit share and a SA return is prepared for them either by the finance manager/director or an Agent.
- The individual SA returns are usually prepared by a senior finance manager to protect the partners' financial confidentiality. The individuals' returns are sent to the partners for completion, adding extra income, expenses or reliefs that are external to the partnership and for checking and signing.
- They are then returned to the Finance Manager (or an Agent) for submission to HMRC through the Government Gateway. One of the law firms estimated that to prepare and submit 130 partners SA returns took two months of their time. This is partly because the Finance Manager must chase partners for their SA returns, a view echoed by both law firms.

The Limited Liability Partnerships (LLPs) that took part in the research said the process of reporting ITSA was their most complex. The main pinch point raised was the need to conduct manual checks and/or adjustments made through separate spreadsheets to prepare their data.

Large business partnerships also raised the following additional pinch points:

- A lack of sophisticated software on the market that deals with IT for partnerships efficiently.
- Partnerships currently reported using bespoke software for IT, which was software that the partnerships built themselves rather than customised 'off-the-shelf' software.
- Complexity was perceived to be compounded by the volume of partners in the business.
- Timeframes: Businesses explained how their accounting year and tax year for individuals was not aligned which led to further complexity.

4. Current and Future Digital Interactions

This chapter explores businesses' current interaction with HMRC, in particular businesses' digital interactions with HMRC, as well as their views towards MTD.

Businesses generally felt that HMRC's current digital offering meets their needs, and did not consider current digital interactions with HMRC to be particularly burdensome. There were some concerns around process issues such as problems experienced uploading data to Government Gateway or having issues with HMRC system log-ins. There was an appetite for moving towards digital ways of working and for HMRC to develop more functionality and interactivity into the current Government Gateway which businesses believed could increase efficiency.

At the time of the research, March to April 2017, businesses' (mid-size and large) awareness of MTD was low, and those that were aware of MTD were generally unclear of the details. Generally, businesses thought the move to digital was positive and were broadly supportive of the principle of interacting digitally with HMRC.

There was a consensus among businesses that they did not have enough information about MTD. Businesses reported HMRC could support them in terms of MTD by providing them with more detail.

4.1. Current interactions with HMRC

Businesses tended to be satisfied with their relationship with HMRC and did not consider the issues they reported to be major. There were however some ways in which businesses thought digital interactions with HMRC could improve further.

Mid-size businesses in particular reported negative experiences of HMRC helplines, and found agent lines better than general helplines. The main issues were getting in touch and finding the person with the technical knowledge to answer their queries.

Businesses thought that it would be more effective if call centre advisers were able to view and share a screen with customers where information about the business was centralised to enable more efficient conversations and problem solving. It was also perceived that the Government Gateway was currently 'read only', and large businesses felt it could be improved by being more actionable. These large businesses explained they can get information from their portal but that they often need to relay this to their CCM who then takes the appropriate action, however, they suggested that being able to take this action themselves on the portal could negate this and help to free-up CCM resource. A specific example of this included:

- A manufacturing business that discussed trying to make an overpayment – there was an appetite to try and request this online but the business felt the only way of achieving this was through the CCM. They also referred to the process for flagging dormant companies/reactivating old ones; ideally, they would like to see a drop-down box on the portal rather than having to arrange this through the CCM.

> *"What you find is you can't actually do anything on the online portals. There isn't very much interaction and if that could be opened, that would make compliance much easier and quicker."*
>
> ***Part of larger UK group, 1000-4999 employees, Manufacturing***

A few businesses also mentioned encountering issues whilst uploading data to the Government Gateway.

For businesses that use the same VAT rates all the time, VAT is relatively easy to manage. However, businesses that are importing or exporting different products all the time found that identifying the correct VAT rates could be problematic. This was compounded by the perception for some that HMRC staff were unwilling to help with deciding which VAT rate should apply, or different staff members providing conflicting information. A perceived lack of flexibility on HMRC's part, particularly in relation to the submission of VAT returns was also communicated.

Moreover, a view echoed by several businesses was that providing all the information to HMRC, including EC sales[17] and Intrastat[18] is inefficient as essentially the same information is being provided but in different formats, none of which have any benefit to the business. Online submission was thought to be more efficient. However, currently, most accounting systems do not seem able to undertake the necessary VAT calculations, adjustments[19], or provide information in the correct format for online submission.

Businesses indicated that where they have more complex financial accounting, such as group structures, subsidiaries and multiple payrolls they are required to manage multiple HMRC system log-ins. Not only is there a perceived security issue in their management but the plethora of log-ins means it is open to error with financial information being uploaded to the incorrect HMRC account. Applying for HMRC system log-ins was also seen as fairly antiquated: applying for an account and a password and receiving this via the postal system was seen to be inappropriate, inefficient and lengthy in the digital age. Businesses thought there might be lessons learned from banks and other suppliers that use faster account opening procedures.

4.2. Awareness and current views on MTD

Businesses were generally aware of MTD in terms of the move to more digital services. Most had heard about the initiative through a variety of sources including: HMRC, tax agents, industry groups, professional magazines, accountancy websites and courses, and the media (e.g. newspapers and radio). Large businesses most commonly heard about MTD from HMRC whereas for mid-size businesses, it was more from the general press including budget summaries, and

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[17] There are various additional reports which need to be filed in the EU to supplement the VAT return. The most commonly required of these supplementary reports is the EC Sales List (ESL). This listing, filed either monthly or quarterly, provides details of sales or transfers of goods and services to other VAT registered companies in other EU countries.
[18] Intrastat is the name given to the method of collecting information and producing statistics on the movement of goods between Member States of the European Union (EU). Please note: Intrastat should not be confused with EC Sales lists which are used to collect information on all sales from UK VAT registered traders to VAT registered traders in other EU Member States.
[19] It was clear that some businesses were able to make adjustments to VAT within their accounting software, so it may be that either other businesses do not have software with this facility or have chosen to operate in a different way.

through accountancy courses and magazines. Whilst some businesses could provide some information about the initiative unprompted (e.g. when it will be introduced and what taxes it will impact on), there was a consensus among businesses that they did not have enough information about the scheme (and how it will work in practice at a granular level) at the time of fieldwork (March 2017).

Those businesses with limited knowledge were broadly positive or neutral. They tended to communicate that digital offered the prospect of making taxes 'more efficient' by reducing paperwork, addressing problems caused by records being lost in the post, and offering greater clarity for businesses on their tax liabilities. Businesses viewed MTD as a continuation of HMRC's recent drive towards online services, such as Real Time Information (RTI) for Payroll, which was considered to be a positive development.

> *"Generally it is a good thing; [there's] no reason why it couldn't be done sooner."*
> ***£3-10 million turnover, 20-49 employees, Property developer***

Those businesses with knowledge beyond the fact that MTD represented a move towards 'digital' tended to be more concerned, primarily because they were aware of and concerned about quarterly reporting. Scepticism was in part driven by uncertainty about what businesses would be required to submit and whether this would increase the burden of reporting.

Businesses stated that they did not know enough about MTD to give fully-informed details about how it would impact on their current processes and systems. The lack of detail presented raised questions among businesses about what was required from quarterly reporting and real-time.

They requested that HMRC give them more detailed information about MTD (and how they envisage it to work in reality) as soon as they possibly can to address any concerns they may have about the initiative and to allow them to start to think about how it will impact their business.

Due to the length of time required to make changes, businesses felt that MTD should be implemented over a longer period. In addition, they expressed a preference for the initiative to be tested iteratively (some stated that they do not have the resource to test too many changes at once).

> *"Don't get this wrong, it's not like we're against the whole idea. This is the direction of the future, we're not against the concept but it's just that implementing it needs to be a much slower, more collaborative and interactive process than it has been."*
> ***Part of a larger UK group, 5000+ employees, Business Services***

4.3. Opportunities and barriers

Overall businesses who were positive about the scheme communicated a number of opportunities associated with MTD. These included:

- Quicker and greater efficiency for dealing with tax affairs, by reducing paperwork;
- Easier and simpler processes for dealing with tax affairs;
- Greater clarity for businesses on their tax liabilities;

- A more holistic view of tax processes, with all their obligations presented in one place, offering greater transparency and a single log-in;
- Large businesses felt there was an opportunity for HMRC to work collaboratively with large businesses in various sectors to understand how MTD should be implemented for different industries;
- Large businesses expressed that MTD would be an opportunity to streamline businesses' interactions with CCMs.

Businesses communicated that they had a lack of detail about MTD and this resulted in a range of concerns associated with MTD. These included:

- Quarterly reporting: there was some concern about how much information would be required and whether businesses would have to pay taxes more regularly – in particular, for CT as businesses communicated that this can be difficult to predict and provide information on;
- The meaning of 'real time' and what this means in practice: businesses asked how often information would be required and what level of information. They questioned whether tax information could genuinely be real-time given that they would be reporting quarterly. This led some businesses to question whether HMRC actually intended for businesses to report monthly, rather than quarterly, increasing concern about the burden involved;
- Whether HMRC's systems would be fit for purpose and whether businesses would have time to upgrade their systems: businesses were concerned that systems and processes would be rolled out before they had been properly tested and piloted which would create burden for businesses when meeting requirements. Businesses stated that they would need a significant amount of time to make and test any changes that may be needed;
- Software incompatibility: there was some concern that existing software packages would not be compatible with HMRC's systems and that providers may seek to profit from the changes by upselling new products;
- Increased resources and costs: businesses were concerned that the changes may create extra work and costs for businesses. There was particular concern about how to predict profits more regularly (particularly for seasonal and overseas work) and whether businesses would be penalised by HMRC for submitting inaccurate reports.

4.4. Making the transition to MTD

Businesses generally found it hard to conceptualise how MTD would work in practice and therefore struggled to express their support needs and expectations.

Nevertheless, businesses presented their ideas as to the expectations and functionality of MTD:

- A simple, joined up and fully integrated system where businesses could access one online account displaying all tax-related information;
- A user-friendly interface/dashboard for the online account;

- HMRC to work with software providers to ensure compatibility and tailored solutions where necessary;
- New systems to be fully tested and piloted before launch;
- Ability to share screens with HMRC call centre advisers to discuss the account;
- Ability to annotate and flag issues on the online account for advisors to see;
- Should be similar to Real Time Information (RTI) for PAYE, with a direct feed from the accounting software;
- Should be able to provide an internal audit that would check for inconsistencies, including data verification.

Businesses voiced additional needs relating to the ways in which HMRC could support businesses during their transition to MTD:

- Simple instructions and clear advice and guidance on what is required;
- A transition period which gives businesses slack to adapt to the new system;
- Training and support offered to businesses before the launch (e.g. webinars);
- A desire for more flexible deadlines around submissions.

How could HMRC communicate with businesses about MTD?

- Clarity on why HMRC is launching MTD; in particular, reasons for implementing quarterly reporting;
- Reassurance that businesses’ existing software will be compatible and that HMRC rigorously tests their software and thinks about the different types of software that businesses use;
- Clarity on what is required and when: a road map for MTD including timelines and internal deadlines.

5. Conclusions

The research demonstrates that the process of reporting taxes differed considerably for complex businesses depending on a number of factors. These included the business structure, being foreign owned/foreign trading, and having group structures and types of ownership (e.g. joint ventures).

Across all business sizes, the tax processes involved a mix of manual and digital tax methods. The research shows businesses are transferring data across multiple systems and software, and that detailed checks are carried out internally and externally by finance and tax professionals before the information is submitted to HMRC. Businesses felt they had the systems and staffing in place to successfully manage the tax reporting processes. Despite this, businesses recognised that their existing information technology systems were not completely efficient in the sense that they often involved a lot of manual checking but were willing to cope with this given that they allow them to accurately report tax information.

Businesses were generally satisfied with their relationship with HMRC although felt the interaction with HMRC could be improved. Some of the suggested improvements related to the Government Gateway such as it being more interactive and issues experienced with uploading data through the Government Gateway.

Levels of awareness of MTD varied considerably, however generally businesses did not feel they had clear detail on what MTD meant in practice. Businesses expected that the new digital system will be designed and tested in close collaboration with them to ensure that MTD considers the following areas of complexity:

- The nature and volume of transactions undertaken by businesses, particularly in terms of VAT where some products/services might be zero rated and others not zero rated;
- The international dimension of business: many transactions will be in different currencies;
- Ownership structure, some of the businesses are responsible for overseeing the reporting of over 50 individual businesses.

Whether or not a business identifies as complex, they struggle, firstly, to see tangible benefits of MTD to their business and, secondly, to express ways in which it could be made to work for them. This was, in part, due to fairly low levels of awareness and understanding of MTD, but also reflected concerns about the possible upheaval involved in any HMRC driven change and the impact this could have on their business.

How is software being currently used by businesses and is there any opportunity to use software to increase efficiency?

The businesses participating in the research used a wide variety of software. At the larger end of mid-size and large businesses, businesses tended to use a software approach they referred to as ERP (Enterprise Resource Planning), which allows an organisation to use integrated applications to manage the business and automate many back-office functions related to technology, services and human resources. Mid-size businesses tended to use off-the-shelf software while large businesses tended to predominantly use customised software to better meet their needs. Whilst businesses generally felt that the systems they had in place worked well, they recognised a number of areas that could be improved.

Spreadsheets were also commonly used in the reporting process - for tasks including formatting/manipulating data, coding/look-ups and accuracy checks. In many cases the spreadsheets had been developed in-house with templates/macros and formulae built in to make the processes more efficient.

The complexity of mid-size and large businesses (and of VAT, CT and IT rules themselves) means that some businesses are not confident that their current processes can be fully automated. Whilst the manual parts of their current processes were not always described as efficient, they were reported to be effective and a vital part of ensuring that the business is compliant.

What aspects of HMRC's digital offering are working well and what lessons are there to learn for MTD?

Overall businesses agreed that the current digital services offered by HMRC were meeting their needs and delivering against expectations. The Government Gateway was perceived to be a very useful tool for transferring information between the business and HMRC (and vice versa). However, there was an appetite for HMRC to develop more functionality and interactivity into the current Government Gateway which businesses believed could increase efficiency.

Businesses were supportive of the principle of interacting digitally with HMRC. They also described broadly positive experiences of using digital processes to file reports and submit payments. However, they struggled to relate these positive views to MTD, or indeed any future changes to managing their tax affairs, primarily due to concerns that changes would exacerbate current inefficiencies in how they manage their tax affairs, which in turn limited their ability to visualise any future benefits. Businesses reported that HMRC should provide more detail on the MTD requirements, allow a transition period for adapting to the new changes and work collaboratively with them to understand how MTD should be implemented in complex businesses.