



Backing business growth study

December 2017

Exploring the role of tax for growth

kpmg.com/uk/tax



Introduction

Welcome to the first backing business growth study, exploring the role of tax for growth.

As a determined supporter of small and medium-sized enterprises (SMEs) in the UK, part of our mission is to source and share the kind of intelligence and insight that can enable leadership teams to make investment decisions with confidence.

Despite making up 99.9%¹ of all private sector businesses and contributing 47% of all private sector turnover², we know that SMEs can often feel overlooked in the general debate around tax.

That is why we have commissioned this survey, which aims to uncover the attitudes of the wider business community – beyond large corporates – towards the UK tax system and give them the voice they deserve.

We spoke to 700 respondents, from CFOs to CEOs and business owners, at businesses with annual revenues from £25 million up to £300 million. The survey covered businesses from a range of ownership structures, including both private and publically listed companies.

We targeted businesses up-and-down the country, from the South West to Scotland, and surveyed 11 business sectors – from manufacturing to media, and from hi-tech to healthcare – to see how opinion varies between those established sectors that are core to the economy, and the emerging industries that are tipped to drive prosperity going forward.

It was heartening to find that a clear majority of respondents recognise that the UK tax system is designed to help this vital part of the economy. But also, they understand that the effective management of tax affairs is an opportunity to foster growth.

The survey found that businesses appreciate that incentives, credits, reliefs and allowances are made available to support their investment, helping them address the low productivity that is denting our international competitiveness, while supporting growth activities like R&D.

But we know that firms in Wales, the North East and Yorkshire, for example, invest far less in R&D than those in the South East and the East³, presenting an opportunity for further activity.

A significant minority also feel that the tax system is too complex, which can deter them from taking full advantage of the incentives available. KPMG's recent report, [Improving UK Regional Productivity Performance](https://assets.kpmg.com/content/dam/kpmg/uk/pdf/2017/11/improving-uk-regional-productivity-performance.pdf), found a direct relationship between regions with lower R&D expenditure per head and poor productivity performance.

We're here to help businesses with the advice they need to help maintain support from the tax system, while also helping to ensure all their arrangements stand up to scrutiny.

We're proud to stand up for small and medium-sized businesses and their interests. We're here to help them navigate their way through the opportunities and threats that pervade the current trading landscape.

Mike Linter, Partner,
KPMG in the UK

^{1,2} <http://www.fsb.org.uk/media-centre/small-business-statistics>

³ <https://assets.kpmg.com/content/dam/kpmg/uk/pdf/2017/11/improving-uk-regional-productivity-performance.pdf>

We surveyed

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sectors



Key findings

Tax is recognised as a driver for growth. That was the fundamental message we received from the businesses we surveyed.

Business leaders leverage the support that exists within the tax regime, appreciating that the incentives and reliefs available have been designed to help companies grow and, ultimately, build a stronger economy for everyone.

Encouragingly, a clear majority (78%) of respondents agreed that the management of tax affairs is an opportunity to support a business' growth. Most of the businesses clearly back Government tax strategy, with 71% agreeing that the tax system is designed to help SMEs succeed and contribute to economic growth.

Indeed, a sizeable proportion (41%) of respondents identified growth as their main motivation in managing their tax affairs, while only a quarter said that it was to ensure compliance (24%) and just a fifth (19%) said that it was to protect their bottom line.

Furthermore, nearly half (48%) identified job creation as the greatest opportunity provided by tax policy, ahead of improving the bottom line (39%), investment in capex (35%), supporting exporting (29%) and attracting investment (26%).

Clearly, attitudes towards tax are progressive, though there remains more work to be done.

In particular, the Government must address SMEs' concerns over complexity and a feeling that policy is too readily shaped by large corporates.

Some 38% of respondents feel tax rules are too complicated, a feeling that was shared in regions outside of London and notably in the North of England, South West and Wales.

And while 72% of firms believe large multinational corporations have too much influence on UK tax policy, 59% felt that the voice of the SME community had been adequately heard. However, in the North this falls to 48%, while among smaller firms with a turnover of £25m-£49m, it dwindles to just 19%.

This perception of complexity, inflexibility and systemic bias means that, while three quarters (73%) of all respondents believe they were making maximum use of the tax system for their business, only 44% of the smallest firms – with revenues between £25m and £49m – share their confidence.

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Tax as a driver for growth

The UK corporate tax regime exists partly to collect revenues to fund our public services, but it also has another important function – to help business and the economy thrive by encouraging support and investment.

Our tax system should aim to support businesses of all sizes as the Government seeks to diversify and rebalance our economy. The study found that many businesses recognise that the management of their tax affairs is an opportunity to support growth in their business, such as accessing support through reliefs and incentives.

And a large proportion said growth is the main motivation for managing their tax affairs, more so than just focusing on compliance or protecting the bottom line.

When we dug a little deeper to examine the objectives that management teams were targeting, job creation was a stand-out ambition. Employment came well ahead of improving the bottom line, investment in capital expenditure, attracting investment and supporting exporting.

While businesses largely appear to back tax as a lever for growth, there is some disagreement over whether tax policy is doing enough to support SMEs already.

Just under half (47%) agree that tax policy encourages entrepreneurship and attract equity investment to SMEs, while over a quarter (27%) say the tax system doesn't do enough.

This view is even more strongly held by the smallest firms. Most companies (61%) with turnovers between £25m to £49m said that the system doesn't do enough, which was echoed by media and entertainment (53%) and healthcare (43%) sectors.

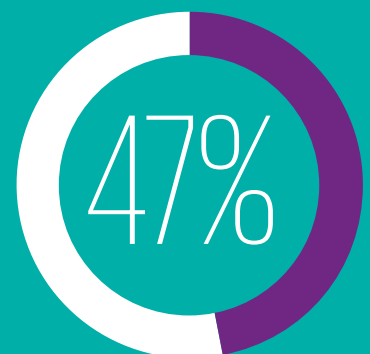
By contrast, there appears to be far less dissatisfaction with the support the tax system provides to the telecoms (13%), automotive (14%), financial services (14%) and hi-tech sectors (17%).

Another element we considered was how well businesses felt that they had made use of the tax system. While many (73%) think they are doing their best to maximise the support available within the tax system for their business, that sentiment varies by sector.

The automotive (86%), financial services (85%) and transportation (82%) sectors seem most engaged and confident in the effectiveness of their tax strategies.

And there was substantial variation among firms of different sizes too, with 87% of larger firms with a £100m to £199m turnover said that they were making maximum use of support on offer, against 44% of smaller firms with a turnover between £25m and £49m.

Clearly, growth is on the agenda for businesses. There is an opportunity to do more in helping management teams better understand and access the tax system to support their objectives.



agree that tax policy is doing more than enough to encourage entrepreneurship and attract equity investment to SMEs



think they are doing their best to maximise the support available

Expertise and influence: SMEs and tax policy

The UK has one of the most voluminous tax codes in the world, more than 20,000 pages long, and there is no doubt that it can take a certain degree of expertise to navigate.

Many businesses often lack the kind of in-house experience needed to fully capitalise on the support that is on offer from the Government.

That may explain why there is still significant dissatisfaction with how the tax regime seeks to support SMEs in contributing to economic growth.

When we asked firms how they would describe current UK tax regulations, over a third criticise them as too complex (38%) while a quarter (24%) say they are too rigidly applied and enforced, though 38% say they are 'about right'.

Perhaps surprisingly, it is the financial services and business and professional services sectors that tell us they find tax rules the most complicated (all 46%), which are the same sectors with the lowest degree of satisfaction with tax policy (31% and 29% respectively).

And while half of smaller firms with a turnover between £25m and £49m say tax rules are too complex, this falls to 32% among larger firms with turnovers between £100m and £199m, perhaps because more modest enterprises are less likely to have in-house tax expertise.

Reassuringly, most firms (69%) agree that the UK tax system is keeping up to date with new services, products and business models in the economy.

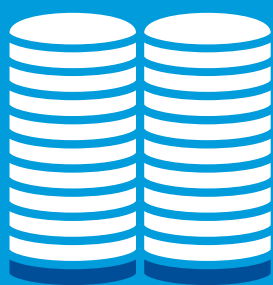
A smaller majority of businesses (59%) are confident that the current tax system allows their business to compete against more disruptive business models, though this falls to 47% in the business and professional services sector and 41% of media and entertainment firms.

Most strikingly, SMEs seem to feel a disconnect with tax policymakers, who they feel are overly influenced by larger global corporates.

Nearly three quarters (72%) tell us they believe multinational corporations have had too much influence on UK tax policy, while just 59% reckon SME's voices have been adequately heard – this figure fell to below half the sample for respondents in the North of England.



We asked firms what they think the take-up rate is like for R&D tax credits



14%

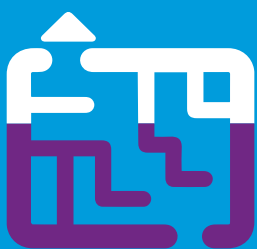
think it's too low



52%

think it's 'about right'

Reasons for the low level of take-up



64%

think complexity is to blame for the low level take-up



23%

say they are too time limited

Incentivising innovation

They say necessity is the mother of invention, but in the UK the tax system has also helped to foster generations of innovative activity.

The regime includes multiple breaks for entrepreneurial enterprises that have helped the country become a hub for entrepreneurs, supporting start-ups with growth potential as well as innovation and job creation in long-established businesses.

Initiatives like Patent Box, which enables companies to pay a lower rate of Corporation Tax on profits earned from its patented inventions, have helped to build businesses that are achieving global success.

But, while the Government has worked to simplify enterprise incentives like R&D tax credits, these developments have not been widely publicised, which could be a factor holding back firms from applying and taking them up.

This is borne out in [KPMG's recent Productivity Report](#), which highlights a significantly lower spend per capita on R&D versus the UK average in certain geographies, such as the North and Wales, which also happen to have a much lower propensity to export.

Still, when we asked firms what they think the take-up rate is like for R&D tax credits, only 14% think it is too low, while over half (52%) think it is 'about right'.

Satisfaction with the regime is highest in automotive (74%) and telecoms (71%), perhaps because these industries have long been involved in 'traditional' R&D activities.

But firms should be aware that R&D comes in many shapes and sizes and many respondents still think they do not qualify. There is a very broad definition of activities that can benefit from R&D tax credits – not just scientists in white coats working laboratories.

For example, a project can be eligible if it researches or develops a new process, product or service, or improves on an existing one. R&D tax credits can even be claimed on unsuccessful projects.

SMEs can also deduct up to 230% of their qualifying R&D costs from their taxable yearly profit. There is no doubt that the process can be complicated, so bringing in expert advice can more than pay for itself.

Complexity is blamed by almost two thirds (64%) of firms for the low level of take-up of R&D tax credits in the business community, while 23% say they are too time limited.

More worryingly, 13% of all firms feel R&D tax credits are "not worth the effort", a view which rises to 31% in the manufacturing and engineering sector, and 50% in the telecoms industry.

The message is clear: businesses still need a more simplified system for R&D incentives. But, there must also be more focus on making sure that all businesses see and appreciate that these initiatives are relevant to them and how they can be used.

Sharing success: Employee ownership and more

Employee ownership has proved successful across a range of sectors in the UK, from retail to manufacturing, with respondents reporting that staff are more motivated to build stronger businesses when they know they stand to receive a share of the wealth they help to generate.

It is something the Government wants to encourage, and it has consulted on simplifying company law to help increase employee share ownership.

As well as fostering and rewarding loyalty, employee ownership also represents a more tax-efficient way of rewarding colleagues.

We wanted to test whether there was much appetite for this type of structure among UK SMEs, so we asked them whether they believe companies that operate employee-share ownership schemes have greater levels of employee engagement than those that didn't?

Over three quarters (76%) agreed, and four in five (81%) firms told us that they would be more likely to adopt employee ownership if the process was simpler.

This isn't surprising. Employee ownership is complex, but deliberately so.

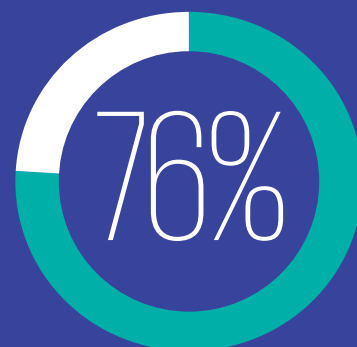
HMRC has rightly applied many checks and measures around these arrangements to ensure that they are not abused.

However, there are plenty of alternatives to 'true' employee ownership that can achieve the same link between business performance and employee reward, effectively improving workforce engagement, but without the complexity. One well-recognised route to achieving the same ends is offering employees fringe benefits, such as group insurance or an enhanced pension plan, in addition to their pay packet.

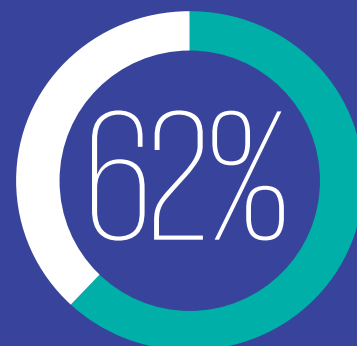
Almost three quarters (74%) of our respondents already provide additional benefits to staff beyond standard remuneration, whether through a flexible benefits package or otherwise.

While 40% judge the taxation system for employee benefits to be complex, over half (55%) think it's 'just right'.

And it seems to be paying dividends, with 62% reporting that the current taxation system for employee benefits is supporting their ability to train, recruit and retain staff.



believe that companies that operate employee-share ownership schemes have greater levels of employee engagement



report that the tax system for employee benefits supports their ability to train, recruit and retain staff

Recommendations to Government

Small and medium sized enterprises (SMEs) are the backbone of the UK economy. Their role in improving innovation and enterprise is crucial, as the UK adjusts to life outside of the European Union.

A competitive and simple tax system will help SMEs to flourish in this new world. This is why we have written to the Chancellor of the Exchequer to share the findings of this campaign.

As the Government looks to create a more inclusive economy, we believe there is now a need to promote SMEs of all sizes – and from all parts of the country and industry – into a bigger role in the policy process. Such a refocus is crucial in rebalancing the UK economy for a sustainable future. Our research has unearthed opportunities that accelerate that process, and our conclusion is clear: the creation of a SME tax task force.

The task force would formally consult with representatives from SMEs, Government, industry associations, regional leaders, and professional services to help develop tax policy in a post-Brexit Britain, identifying effective ways to raise awareness and understanding of the opportunities provided by the tax system.

We stand at a critical juncture in preparing for our new life outside of the European Union. It is more important than ever that the Government uses this opportunity to unleash the potential of our SME community. At KPMG, we are committed to supporting the Government in delivering this potential.

We know that SMEs are the engine for enterprise and growth across the UK.

We hope that others from the across the business world will add their weight, experience and expertise to this vital initiative, and make that engine roar.



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