

Is tax a moral or legal debate?

Tax and the responsibilities of business are once again making headlines with the debate centred upon the legitimacy of tax planning.

The reason why we all pay tax is to finance the State and the services it provides. For example, access to healthcare, education, law enforcement are all designed to support the common good and help create a more balanced and caring society.

Tax evasion, the practice of deliberately setting out not to pay the right amount of tax by such means as omitting income, overstating expenditure, failing to declare a capital gain or not declaring sources of taxable overseas income, is obviously illegal.

Legitimate legal devices encourage business growth

Whereas tax mitigation, through following the letter and spirit of UK legislation – ‘tax planning’, — is an entirely legitimate activity that companies (and individuals) undertake in order to minimise their liability. This manifests itself through taxpayers using regulations that successive governments have made available to reduce their tax bill.

At a corporate level tax planning can take the form of such things as being able to deduct the cost of machinery against taxable profits, or using the Research and Development tax credit scheme, which encourages innovation and increased spending on R&D activities by allowing such spending to be tax deductible. It’s important to recognise that very often such legitimate legal devices are introduced in order to benefit society through encouraging business growth or providing support to industries that are vital to the country.

Individuals manage their tax affairs in a similar manner

On an individual level, many of us also take advantage of ISAs and tax free pension contributions allowing us to hold on to more of our money for longer. This is perfectly legal and a sensible way for us to manage our financial affairs.

It is tax avoidance; the more provocative use of tax planning that stimulates the most debate. This can best be defined as businesses (or individuals) seeking to gain a tax advantage through the literal interpretation of legislation in a way for which it wasn’t necessarily designed. A common hallmark of tax avoidance is that highly artificial steps have been inserted into a transaction in order to achieve the desired outcome.

The practice of identifying strategies and loopholes to avoid paying tax is certainly not illegal. However it is debatable as to whether or not it’s moral. While it has to be acknowledged that businesses have obligations to shareholders to maximise profit, they also have obligations to be honest and transparent.

The whole area of morality in tax; what is legitimate tax planning compared to what is egregious tax avoidance is so subjective that it is hard for a consensus to be reached on what is socially acceptable. In the absences of such certainty, it is perhaps understandable that the public are asking the question, is this the right way to do business?

Acting unethically or with a lack of transparency can damage a business’ reputation and it is prudent to take measures to prevent against this. Before engaging accountants and tax advisors, businesses should always discuss their ethical stance in respect of tax matters to ensure it is in line with their own organisation’s core values.

The Great Business Debate

Out of recognition that there is growing public mood for greater transparency in the tax system, businesses are increasingly choosing to publish a tax policy statement as part of their corporate reporting. With ethical behaviour of businesses under increasing scrutiny, a more transparent approach could be the best way forward.