HM Revenue & Customs

Issue briefing

Taxing the profits of multinational businesses

Recent stories in the media have suggested that some high-profile multinational businesses do not pay their fair share of corporation tax on profits they make from their business with UK customers. This briefing explains how the profits of multinational businesses are taxed, and how tax policy affects where multinationals choose to locate.

Paying a fair share of tax

Everyone – businesses as well as individuals – should pay their fair share of tax as intended by Parliament. The vast majority of individuals and businesses do pay the right amount of tax at the right time, and HMRC strives to maintain a level playing field for businesses by tackling the minority who try to dodge tax.

HMRC is alive to the risk that multinationals may try to structure their affairs so that profits from economic activity carried on in the UK are not taxed here. There are tax rules designed to combat tax avoidance by multinationals and HMRC deploys specialist tax professionals to ensure that multinationals comply with the rules.

How multinational businesses are taxed

Most multinational businesses are not set up as a single company, but as a group of companies, only some of which will be operating in the UK. In broad terms, companies are required to pay corporation tax in the country where they carry on the economic activity that generates their profits, not where their customers are located. Many elements contribute to a multinational business's economic activities including: sales, employees, technology, physical assets and intellectual property. Tax rules need to establish how much of a business's overall activities should be treated as 'belonging' in a particular country. This is different from VAT, which normally depends on the location of the customer.

Why location is important

A UK-resident company has to pay UK corporation tax on the profits from its UK activities. A company which is not resident in the UK does not have to pay UK corporation tax on its trading profits, unless it is trading through a branch in the UK. Having UK customers is not the same as having a branch in the UK.

Non-resident trading companies which do not have a branch in the UK, but have UK customers, will therefore pay tax on the profits arising from those customers in the country where the company is resident, according to the tax law in that country. The profits will not be taxed in the UK. This is not tax avoidance: it is simply the way that corporation tax works.

Most major economies operate corporation tax in the same way as the UK, so UK-resident companies are treated in a similar way in other countries. In other words, UK companies do not pay corporation tax to another country on the profits from sales in that country, unless they trade through a branch based there. Instead, they pay corporation tax in the UK.

Our approach

International tax law is complex and HMRC works closely with tax authorities across the world to promote the adoption and consistent operation of tax rules that result in a fair and joined-up tax system.

In common with most of our major trading partners, the UK has 'transfer pricing rules' which ensure that UK profits are not reduced by the mispricing of transactions between companies in a group. There are also anti-avoidance rules, known as 'controlled foreign company (or CFC) rules', which prevent groups based in the UK from shifting profits from significant UK-based activities to a country with a lower tax rate.

HMRC seeks to develop open and co-operative relationships with multinational businesses. In the vast majority of cases, we can reach agreement about what the right amount of tax is. Where we cannot reach agreement, we take a robust approach and take large businesses to court, where necessary, to secure the right amount of tax.

International tax competition

Globalisation means that multinationals have the opportunity to structure their business to take advantage of beneficial tax rules in different countries. Provided that this results in profits being taxed in line with where genuine economic activity is carried on, this does not amount to tax avoidance. Recent reforms to the UK's corporation tax system mean that the UK has an internationally-competitive corporate tax system, which is designed to attract and retain economic activity here.

Some countries which aim to attract multinational businesses have tax policies that are harmful to others. The UK's existing tax rules provide a strong defence against tax avoidance, and the UK also works to achieve an international consensus by actively contributing to discussions in the European Union and the Organisation for Economic Co-operation and Development (OECD). This puts international pressure on countries with harmful tax practices to reform their policies.

Identifying how much corporation tax is paid

Company accounts include references to tax liabilities, but it is not generally possible to identify from the accounts how much UK corporation tax has been paid. This is because of the differences between the way in which profits are calculated for the accounts and the way that they are calculated for tax purposes. So although an apparently low tax rate in a company's accounts might indicate tax avoidance, it could also be the case that the business has acted entirely properly, by making use of specific tax reliefs and incentives designed, for example, to encourage capital investment or research and development.

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