



House of Commons
Committee of Public Accounts

HM Revenue & Customs: Annual Report and Accounts 2011–12

Nineteenth Report of Session 2012–13

*Report, together with formal minutes, oral and
written evidence*

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Committee of Public Accounts

The Committee of Public Accounts is appointed by the House of Commons to examine "the accounts showing the appropriation of the sums granted by Parliament to meet the public expenditure, and of such other accounts laid before Parliament as the committee may think fit" (Standing Order No 148).

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Mr Justin Tomlinson (*Conservative, North Swindon*)

The following Members were also Members of the committee during the parliament:

Dr Stella Creasy (*Labour/Cooperative, Walthamstow*)
Justine Greening (*Conservative, Putney*)
Joseph Johnson (*Conservative, Orpington*)
Eric Joyce (*Labour, Falkirk*)
Rt Hon Mrs Anne McGuire (*Labour, Stirling*)
Matthew Hancock (*Conservative, West Suffolk*)
James Wharton (*Conservative, Stockton South*)

Powers

The committee is one of the departmental select committees, the powers of which are set out in House of Commons Standing Orders, principally in SO No 152. These are available on the internet via www.parliament.uk.

Publications

The Reports and evidence of the Committee are published by The Stationery Office by Order of the House. All publications of the Committee (including press notices) are on the internet at www.parliament.uk/pac. A list of Reports of the Committee in the present Parliament is at the back of this volume. Additional written evidence may be published on the internet only.

Committee staff

The current staff of the Committee is Adrian Jenner (Clerk), Sonia Draper (Senior Committee Assistant), Ian Blair and James McQuade (Committee Assistants) and Alex Paterson (Media Officer).

Contacts

All correspondence should be addressed to the Clerk, Committee of Public Accounts, House of Commons, 7 Millbank, London SW1P 3JA. The telephone number for general enquiries is 020 7219 5708; the Committee's email address is pubaccom@parliament.uk

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Summary

Transparent, predictable and fair taxation is at the core of our public finances. The Government has a responsibility to assess and collect tax due from all taxpayers, without fear or favour, and taxpayers should pay all that tax which is due. Whilst we looked at a range of issues among HM Revenue & Customs' (HMRC's) activities, our principal enquiries were into the corporation tax paid by multinational companies.

The hearings we held showed that international companies are able to exploit national and international tax structures to minimise corporation tax on the economic activity they conduct in the UK. The outcome is that they do not pay their fair share. We believe that this practice is widespread and that HMRC is not taking sufficiently aggressive action to assess and collect the appropriate amount of corporation tax from these multinationals. If companies do not pay their fair share of tax, other taxpayers have to pay more. Both HMRC and corporate taxpayers are failing to meet the legitimate public expectations from the tax system.

We took evidence from multinational companies and HMRC to understand how successful companies with huge operations in the UK pay little or no corporation tax. The evidence we received was unconvincing, and in some cases evasive. We are concerned that multinationals have an unfair competitive advantage over British businesses which have no choice but to pay their corporation tax. It is also unclear whether HMRC has the necessary resources or are devoting the time and effort to collect the appropriate level of tax.

HMRC needs a change in mindset in the way it approaches collecting tax from multinationals. At the moment there is a pervasive acceptance of the status quo by the top officials in HMRC and we have seen little evidence of a desire to be more assertive. For example, it is perplexing that, on transfer pricing HMRC consider a royalty fee of 6% or 4.7% can be competitive when the company involved consistently makes a loss. We expect HMRC to prosecute multinational companies who do not pay the tax due in the UK.

This change of mindset needs also to apply to HMRC's approach to the Tax Gap—the difference between tax collected and that which, in the Department's view, should be collected. While total tax revenues have increased by £4 billion since 2010-11, the Department's own assessment of the gap stands at £32 billion and has only reduced by £1 billion since 2004-05. Despite this poor performance, HMRC were unconvincingly positive about the situation. While we recognise that it will always be an unequal fight between HMRC and multinational companies, HMRC should not be so accepting of failure and should set ambitious targets to reduce it as soon as possible.

There is currently a complete lack of transparency about why multinationals pay so little corporation tax. Global companies structure their companies in ways that are impenetrable to the public and HMRC disclose very little about their approach to collecting tax from them. This undermines public confidence in the tax system and in HMRC which could have a negative impact for wider tax compliance. Effective change may require international cooperation to make sure that the UK is not isolated, but there is a moral case on top of the basic economic case that taxation of economic activity should transparently

reflect where that activity occurs. The UK should be in the lead in making and enforcing this case. There are also steps HMRC and the UK Government can take to improve the legitimate tax take from multinational corporations.

For individual taxpayers, HMRC deserves praise for clearing the backlog of un-reconciled legacy PAYE cases, before its target of December 2012, but is too complacent about the service it provides to customers. The next challenges HMRC faces are the roll-out of the Real Time Information system and the changes to child benefit. HMRC did not convince us that it will manage the potential increase in its workload or that it had fully considered the impact on taxpayers. There are four months to go before the main roll-out of the Real Time Information system. The system is vital for the Department for Work and Pensions' introduction of Universal Credit, but HMRC has no contingency planning to cope with any delays in implementation.

The Department's performance in reducing the level of error and fraud on the tax credits it pays has got worse rather than better, and it has failed to meet its target. In the future, families may find themselves struggling to repay money from much reduced Universal Credit payments as a consequence of the Department's poor performance.

On the basis of a Report by the Comptroller and Auditor General,¹ we took evidence from HM Revenue & Customs on its Annual Report and Accounts 2011-12 and from Amazon, Google and Starbucks.

1 C&AG's Report, *HM Revenue and Customs 2011-12 Accounts*: Report by the Comptroller and Auditor General, Session 2012-13, HC 38

Conclusions and recommendations

1. **The UK Government needs to get a grip on large corporations which generate significant income in the UK but pay little or no tax.** Despite an increase in total tax revenues of £4 billion from last year, corporation tax revenues have fallen. Multinationals appear to avoid UK corporation tax by arranging their corporate structures, transfer payments and royalties to move money to low tax jurisdictions overseas. There is little credible information to inform public debate over the equity of corporate tax payments and HMRC lacked clarity when explaining its approach to enforcing the corporation tax regime. Since multinational companies are able to set up in any country, this may need international co-ordination to resolve. HMRC should work with HM Treasury to:
 - police our tax borders more efficiently, introducing national measures to secure a fair contribution to the tax base from multinational corporations;
 - lead international efforts, particularly within the EU, to reform the way in which multinational companies are able to transfer earnings overseas and thereby potentially avoid tax payments;
 - publish clear sector benchmarks for common charges such as royalty payments and intellectual property rights; and
 - develop best practice standards in the information companies should make publicly available about their tax practices and work with the relevant bodies to make them part of mandatory reporting requirements.
2. **HMRC needs to be seen to challenge practices to prevent the abuse of transfer pricing, royalty payments, intellectual property pricing and interest payments.** HMRC needs a far more determined approach to dealing with multinationals and their tax affairs. Top officials need to challenge the status quo and be more assertive, for example in accepting that excessive levels of royalty payments are appropriate when businesses are making a loss. Given the high-profile cases of large companies avoiding tax and the Department's selective prosecution practice, there may be an impact on the compliance rate of individuals and small and medium companies who feel victimised. HMRC should direct more effort into challenging artificial arrangements, be more willing to prosecute improper corporate arrangements and make more information available to the public about this aspect of its work.
3. **HMRC is too passive in its approach to closing the tax gap.** It has only reduced the gap between what is due and what is collected by £1 billion since 2005. Closing the tax gap is central to public perceptions of fairness during a period of austerity and of cuts to public services and HMRC appears to be complacent in its approach. HMRC must set immediate and ambitious targets to reduce the tax gap.
4. **This Committee lacks confidence that HMRC both has and is using the business intelligence systems it needs.** HMRC is rationalising 3,000 systems down to 13 big systems. Private sector tools for business intelligence analysis develop quickly, but HMRC does not. In 2004, and again in 2009, this Committee recommended HMRC

use risk profiling to better target debt collection activities; but full implementation of systems to enable systematic analysis of debt and of debtor behaviour (known as “analytics”) has been delayed from April 2011 to October 2012. HMRC should use its fully implemented analytics systems to develop a sector-by-sector approach to compliance activity so that it focuses resources on priority areas.

- 5. HMRC is unduly complacent about the rollout of the Real Time Information (RTI) system and the child benefit changes.** We are concerned that, with four months to go to the main roll out of RTI, the project has been rated amber by the Major Projects Authority. The Institute of Chartered Accountants in England and Wales (ICAEW) thinks that the Department’s current plans will increase the burden on small businesses and therefore on the Department’s workload. Similarly more individuals will be required to register for self-assessment as a result of the changes to child benefit. HMRC believes that there will be negligible impact from both sets of changes and do not have contingency plans to deal with delay or fluctuations in workload. By the end of March 2013, HMRC should provide the Committee with details of its plans to manage the burden on small businesses as a result of RTI; and provide credible contingency arrangements should the main rollout of RTI between April and October 2013 not go according to plan.
- 6. HMRC is persistently unable to get a grip of error and fraud in tax credits.** The estimated level of error and fraud in tax credit payments was between £2.08 billion and £2.46 billion in 2010-11, which was higher than both the estimate for 2009-10 and its target. Given its performance, HMRC is unlikely to recover tax credit debt before the introduction of Universal Credit. Families may receive less money from the new system, and will receive even less if they have to repay tax credit overpayments. The poor administration of tax credits will undoubtedly deter some of the most needy from claiming tax credits yet HMRC has not made any estimate of the extent of this. HMRC must improve its use of data and analytics to target its interventions more effectively and improve the accuracy of tax credit awards by the end of 2012-13.

1 Tax avoidance by multinational companies

1. In 2011-12, £474.2 billion of total tax revenue accrued to HM Revenue & Customs (the Department) which was £4.5 billion higher than for 2010-11. Yet there was a decrease in corporation tax revenue of £6.3 billion.²

2. HMRC stated that it had been a policy of successive Governments to make the UK an attractive place for business and for multinationals to see the UK as competitive.³ But HMRC also expected everybody to pay their fair share of tax and saw its role as strictly enforcing the tax laws which it felt were strong enough to collect tax owing under both national and international tax systems⁴ and rebutted any suggestion that it had been lenient with big businesses.⁵

3. We were not sufficiently convinced by the Department's assertion that it was pursuing all the tax due from big businesses given the reduction in corporation tax revenue from last year.⁶ There is genuine public anger and frustration because there is an impression that rigorous action is taken against ordinary people and small businesses and British companies based wholly in the UK but, apparently, lenient treatment is given to big corporations, of which almost half have a head office overseas.⁷

4. HMRC considered that it had a well-resourced unit bringing in very significant amounts of money; for the 770 largest businesses it had 1,200 staff and was able to draw on expertise across the Department, for instance 65 transfer pricing experts.⁸ HMRC told us that it had the right talent: many of its staff resist offers from firms and are motivated by the public service ethos.⁹ We were sceptical of these claims.

5. HMRC was not able to show conclusively that tax avoidance was not increasing.¹⁰ HMRC also could not tell us how many of the big corporations were handling their tax affairs through offshore tax havens but suggested that it could provide figures in future annual reports.¹¹ HMRC told us that all it could do was to apply the law as it is and, in an international setting, multinational businesses could choose, to some extent, where to set

2 C&AG's Report: para 1.3; Figure 1; and Figure 2

3 Qq 20-21

4 Qq 23-24

5 Q 29

6 Q 26

7 Qq 25-26, 29, 33 Ev 50

8 Q 65

9 Q 95

10 Qq 26-28

11 Qq 46-47

up and where some of their profits are based.¹² International co-operation will be required to improve global tax legislation.¹³

6. HMRC acknowledged that it has to maintain broad confidence and credibility in its administration of the tax system to maintain the very high levels of compliance that there is in the UK.¹⁴ However, we felt that this was undermined by the Department's use of selective prosecutions; a practice which it could not clearly justify to the Committee.¹⁵ HMRC had not carried out any analysis into the effect high-profile cases of large companies avoiding tax could be having on the compliance rate of individuals and small and medium companies.¹⁶ Multinational companies appear to be using transfer pricing, payment of royalties for intellectual property or franchise payments to other group companies to artificially reduce their profits in the UK or to remove them to lower tax jurisdictions.¹⁷ We were not convinced that HMRC has the determination to robustly challenge the practices of these companies.

7. To explore these issues, the Committee held a hearing with representatives from three multinational companies (Amazon, Google and Starbucks) and we are grateful to those companies for providing evidence to us. While their circumstances and business models are different they all have a significant commercial presence in the UK and we wished to gain an understanding as to why it appears that they do not pay their fair share of corporation tax in the UK.¹⁸ Our intention in inviting these companies was to provide an illustration of what we perceive to be a wider problem of possible corporation tax avoidance; not to single out Amazon, Google and Starbucks as the only companies engaging in these practices.

8. Starbucks told us that it has made a loss for 14 of the 15 years it has been operating in the UK, but in 2006 it made a small profit.¹⁹ We found it difficult to believe that a commercial company with a 31% market share by turnover, with a responsibility to its shareholders and investors to make a decent return, was trading with apparent losses for nearly every year of its operation in the UK.²⁰ This was inconsistent with claims the company was making in briefings to its shareholders that the UK business was successful and it was making 15% profits in the UK.²¹ Starbucks was not prepared to breakdown the 4.7% payment for intellectual property (which was 6% until recently) that the UK company pays to the Netherlands based company.²² The Committee was sceptical that the 20% mark-up that the Netherlands based company pays to the Swiss based company on its coffee buying

12 Q 25

13 Qq 47-48

14 Q 49

15 Qq 54-60

16 Q 49

17 Qq 25-28

18 Qq 189

19 Qq 190, 204

20 Qq 205-206

21 Qq 190-197, 202,231, 240-253

22 Qq 211-225

operations, with a further mark up before it sells to the UK, is reasonable.²³ Starbucks agreed that it had a special tax arrangement with the Netherlands that made it attractive to locate business there, which the Dutch authorities asked Starbucks to hold in confidence, and that Switzerland offers a very competitive tax rate.²⁴ In addition, there is an inter-company loan between the US Starbucks business and the UK Starbucks business over a period of time with the interest rate set at higher rate than any similar loan we have seen.²⁵ We suspect that all these arrangements are devices to remove profits from the UK to these areas with lower tax.²⁶

9. At the hearing we were frustrated with the representative from Amazon, who we found evasive and unprepared to answer legitimate questions on the company's structure and the true location of its economic activity.²⁷ Amazon has subsequently provided this information.²⁸ Amazon has a reported turnover of £207 million for 2011 for its UK company (Amazon.co.uk), on which it has shown a tax expense of only £1.8 million, however it shows a European-wide turnover of €9.1 billion for its Luxembourg based company (Amazon EU Sarl) and a tax of €8.2 million.²⁹ Amazon.co.uk is a service company in the UK providing services to Amazon EU Sarl for which it receives payment.³⁰ That company is owned by a holding company, which is a subsidiary of Amazon's group companies.³¹ Amazon subsequently provided a copy of the unaudited accounts for Amazon Europe Holding Technologies S.C.S for 2011 showing a profit of €301.8 million and no tax payments.³² Amazon also provided information showing that for 2011, £3.35 billion of sales were from the UK, 25% of all international sales outside the USA.³³ Yet Amazon has over 15,000 staff in the UK, invoices UK customers from the UK, hires UK staff in the UK, has inventory physically in the UK for UK customers and to all intents and purposes has the majority of its economic activity in the UK, rather than in Luxembourg, but pays virtually no corporation tax in the UK.³⁴ Amazon has received an assessment from the French tax authorities which it disputes.³⁵

10. Google explained in its responses that it minimised tax within the letter of the law and that low tax areas or tax havens influenced where it located its group companies.³⁶ The vast majority of Google's non-USA sales are billed in Ireland.³⁷ Google makes money from

23 Qq 257-262, 306

24 Qq 242-245, 273, 285-288

25 Qq 268-270

26 Qq, 289-299, 322-323, 325, 327

27 Qq 368, 383, 391, 399-406, 413-418, 422-426, 434-445, 612-613

28 Ev 57

29 Qq 349, 354-356, Ev 58

30 Q 381

31 Q 389, Ev 58

32 Ev 58

33 Ev 57

34 Qq 344-346, 365-366, 368, 371, 372, 374, 375, 377, 379, 380, 388, 421-422

35 Q 443

36 Qq 454, 472-477, 483-485, 520, 613

37 Q 448

business to business advertising, adverts which can be targeted to the UK website and to UK Google users³⁸. In the UK, Google Ltd recorded revenues of £396 million in 2011, from Google Ireland, but paid corporation tax of only £6 million.³⁹ Google Ireland paid for the services provided by the 1,300 staff in the UK.⁴⁰ Google had approximately 700 staff who undertake marketing work in the UK as part of their activities, but only 200 of Google's Irish staff of 3,000 were involved in marketing Google in the UK.⁴¹

11. Google accepted that profits should be taxed in the jurisdictions where the economic activity generating those profits occurred⁴² but it asserted that its underlying economic activity arose from the innovative software technology underlying its Google search engine generated by the US company.⁴³ Google also confirmed that it had an entity based in Bermuda to protect its intellectual property.⁴⁴ We consider that the company undermined its own argument since it remits its non-USA profits (including from the UK) not to the USA but to Bermuda and therefore may be depriving the USA of legitimate tax revenue as well as the UK.⁴⁵ Subsequently, Google told us that there were no outstanding issues with HMRC about Google UK's accounts. HMRC is currently carrying out a review of the tax returns filed by Google UK for 2005-11 inclusive and Google told us this is standard practice and that it is co-operating fully with that review.⁴⁶

12. All three companies accepted that profits should be taxed in the countries where the economic activity, that drives those profits, takes place and that, alongside their duty to their shareholders, they had obligations to the society, from which they derive their profits, which included paying tax. However, we were not convinced that their actions, in using the letter of tax laws both nationally and internationally to immorally minimise their tax obligations, are defensible.⁴⁷ They all accepted that the perceived ethical behaviour of corporations could affect consumer behaviour. Being more transparent about their business practices, including paying their fair share of taxes, was becoming an increasingly important issue to their customers.⁴⁸

The Tax Gap

13. The tax gap is the Department's measure of the difference between tax collected and the tax that would be collected if all individuals and companies complied with both the letter and the spirit of the law. The Department estimated that some 25% of the tax gap is down

38 Qq 457-459, 511 450

39 Qq 454-455

40 Qq 455, 461, 551-552

41 Qq 461-468, 472

42 Qq 478, 480, 516, 537, 548

43 Qq 456, 469, 478, 501, 516, 535, 539, 548

44 Qq 474 – 476

45 Qq 475-476, 479-483, 486-491, 502, 517, 521-524, 536, 545-548, 575

46 Ev 59

47 Qq 579-587

48 Qq 594-596, 603

to large businesses, although this includes other taxes as well as corporation tax discussed above.⁴⁹

14. HMRC's latest published estimate of the gap for 2010-11 is £32.2 billion which has reduced from £33.3 billion for 2004-05.⁵⁰ HMRC did not agree with the Committee's view that there has been disappointing progress in closing the tax gap as the gap, while trending down only very slowly, is competitive when compared with most countries and is lower than Sweden and the United States.⁵¹

49 *HM Revenue and Customs, Annual Report and Accounts 2011-12* (Session 2012-13, HC 38), Trust Statement Note 1.1 Qq 13-15

50 *HM Revenue and Customs, Measuring tax gaps 2012: tax gap estimates for 2010-11*, Table 1.3, Qq 13-15

51 Qq 13-17

2 Business intelligence and workload management

Business intelligence systems

15. HMRC has not implemented the recommendations we made in 2004 and 2009 to use risk profiling of taxpayers to better target their collection activities. It has delayed fully implementing a project to enable systematic analyses of debt balances and debtor behaviours from April 2011 to October 2012.⁵² HMRC acknowledged that it is not yet making full use of its investment in technology to analyse data. It is moving from 3,000 individual IT systems to a “big 13 systems”. It will only be able to make full use of its data to target compliance activity effectively when that move is complete. It also told us that by then there would be more powerful systems on the market.⁵³

Workload management

16. HMRC met its target to complete the end of year reconciliations for the 2008-09 and 2009-10 tax years by March 2012.⁵⁴ It subsequently cleared outstanding PAYE reconciliations relating to tax years 2003-04 to 2007-08 before its target date of December 2012.⁵⁵

17. In November 2012 HMRC sent out letters about changes to Child Benefit to higher rate taxpayers who may need to join the self-assessment system. It acknowledged that the child benefit changes would be a big change for people affected and that it had found the implementation a challenging piece of work. However, it asserted that it was ready for the increase in self-assessment registrations and returns, the call centres were ready for calls, and the website was easy to use for taxpayers who needed advice on what to do.⁵⁶

18. The next major change for the PAYE system is introducing Real Time Information (RTI), where employers must report employees’ income tax and National Insurance deductions as they pay them rather than at the year-end. The Department for Work and Pensions’ timetable to implement Universal Credit is driving the timetable to roll-out RTI and all employers have to be using RTI by October 2013.⁵⁷ HMRC acknowledges that the Institute of Chartered Accountants in England and Wales (ICAEW) and the Federation of Small Businesses have expressed concerns that many smaller enterprises will find the introduction of RTI onerous and many did not seem to be aware of the new requirements. HMRC told us that it is keen to understand where businesses have a real business dynamic

52 C&AG’s Report, para 3.18 – 3.19

53 Q 99

54 C&AG’s Report, para 2.10

55 Qq 152-153

56 Qq 122-124

57 C&AG’s Report, para 2.25-2.26

that makes it hard to do what it is asking in terms of providing information to the Department.⁵⁸

19. HMRC acknowledged that it still has a lot of work to do and that the Major Projects Authority had rated the RTI project as Amber.⁵⁹ On the 6th November 2012, just over 2 million employment records for 6,827 schemes had been migrated to RTI.⁶⁰ HMRC expects close to 39 million records to have migrated by October 2013.⁶¹ HMRC expressed confidence that it is on track to deliver RTI by October 2013. HMRC also does not have a contingency plan in case RTI is delayed.⁶²

58 Qq 126, 137-141

59 Qq 116-118

60 Qq 131, Ev 51

61 Q 136

62 Qq 145-146

3 Tax credits

20. HMRC had a target to reduce tax credits error and fraud to no more than 5 % of the value of awards finalised by March 2011. However, in June 2012 HMRC announced that it had not achieved this target. It estimated that the level of error and fraud in tax credit payments made in 2010-11 was between 7.5 % and 8.8 %. This level of error was higher than the previous year, when the estimate was between 7.0 % and 8.6 %. In 2010-11 HMRC had made incorrect tax credit payments amounting to between £2.08 billion and £2.46 billion because of error or fraud.⁶³

21. HMRC acknowledged that it was clearly disappointing that the level of error and fraud had not dropped to 5 %.⁶⁴ The assumptions underpinning the target about the deterrence effect of the Department's interventions and the length of time for which an award stays correct were not borne out in practice.⁶⁵ HMRC is working to understand why these assumptions did not reflect reality and expect to, consequently, revisit their strategy in the next couple of months.⁶⁶

22. HMRC is likely to generate a further £1.6 billion in new personal tax credit debt in 2012-13⁶⁷ and, without any further intervention; total debts could increase to £6.5 billion by 2014-15.⁶⁸ This may mean that there will be a further substantial write-off or affected taxpayers will see their new, and in all probability lower, Universal Credit benefit cut at source to make repayments on tax credit debt.⁶⁹ This and the fear of being pursued for overpayments may discourage entitled individuals from claiming tax credits. The Department's latest estimate for the take-up of tax credits show that in 2009-10 around 2.7 million households did not claim tax credits.⁷⁰ HMRC has not done any research on the reasons why people who are entitled to tax credits do not claim.⁷¹

63 C&AG's Report, paras 4.9-4.10

64 Q 154

65 Qq 154-156

66 Qq 156-158

67 Q 163

68 Q 163; C&AG's Report, para 4.28

69 Q 165

70 Ev 50

71 Q 171

Formal Minutes

Wednesday 28 November 2012

Members present:

Mrs Margaret Hodge, in the Chair

Mr Richard Bacon
Guto Bebb
Jackie Doyle-Price
Meg Hillier
Fiona Mactaggart

Mr Austin Mitchell
Nick Smith
Ian Swales
Justin Tomlinson

Draft Report (*HM Revenue and Customs: Annual Report and Accounts 2011-12*), proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 22 read and agreed to.

Summary agreed to.

Resolved, That the Report be the Nineteenth Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

Written evidence was ordered to be reported to the House for printing with the Report (in addition to that ordered to be reported for publishing on 12 November 2012).

[Adjourned till Monday 3 December at 3.00 pm]

Witnesses

Monday 5 November 2012

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Lin Homer, Chief Executive and Permanent Secretary, **Nick Lodge**, Director General, Benefits and Credits, **Simon Bowles**, Chief Finance Officer, and **Edward Troup**, Tax Assurance Commissioner, HM Revenue and Customs

Ev 1

Monday 12 November 2012

Troy Alstead, Starbucks Global Chief Financial Officer, **Andrew Cecil**, Director, Public Policy, Amazon and **Matt Brittin**, Google Vice President for Sales and Operations, Northern and Central Europe

Ev 21

List of printed written evidence

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3	Amazon EU SarL	Ev 56; 57
4	Google	Ev 58

List of Reports from the Committee during the current Parliament

The reference number of the Government's response to each Report is printed in brackets after the HC printing number.

Session 2012–13

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Third Report	Efficiency and reform in government corporate functions through shared service centres	HC 463
Fourth Report	The completion and sale of High Speed 1	HC 464
Fifth Report	The Regional Growth Fund	HC 104
Sixth Report	HM Revenue & Customs: Renewed Alcohol Strategy	HC 504
Seventh Report	Immigration: The Points Based System – Student Routes	HC 101
Eighth Report	Managing early departures in central government	HC 503
Ninth Report	Preparations for the London 2012 Olympic and Paralympic Games	HC 526
Tenth Report	Implementing the transparency agenda	HC 102
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Twelfth Report	Off-payroll arrangements in the public sector	HC 532
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Fourteenth Report	Assurance for major projects	HC 384
Fifteenth Report	Preventing fraud in contracted employment programmes	HC 103
Sixteenth Report	Department of Health: Securing the future financial sustainability of the NHS	HC 389
Seventeenth Report	Department of Health: The management of adult diabetes services in the NHS	HC 289
Eighteenth Report	HM Treasury: The creation and sale of Northern Rock plc	HC 552

Oral evidence

Taken before the Committee of Public Accounts on Monday 5 November 2012

Members present:

Margaret Hodge (Chair)

Mr Richard Bacon
Meg Hillier
Mr Stewart Jackson

Fiona Mactaggart
Austin Mitchell
Nick Smith

Amyas Morse, Comptroller and Auditor General, National Audit Office, **Paul Keane**, Director, NAO, **Marcia Lant**, Financial Audit Director for Department for Work and Pensions, NAO, and **Paula Diggle**, Treasury Officer of Accounts, were in attendance.

REPORT BY THE COMPTROLLER AND AUDITOR GENERAL

HM Revenue & Customs 2011–12 Accounts

Examination of Witnesses

Witnesses: **Lin Homer**, Chief Executive and Permanent Secretary, HM Revenue and Customs, **Nick Lodge**, Director General, Benefits and Credits, HMRC, **Simon Bowles**, Chief Finance Officer, HMRC, and **Edward Troup**, Tax Assurance Commissioner, HMRC, gave evidence.

Q1 Chair: Welcome. We have a huge amount to get through this afternoon. Apologies if we repeat some of the issues that were raised last week at the Treasury Select Committee, but we have not been able to see the transcript of that hearing yet, so inevitably there will be some overlap. I will be grateful for answers that are really succinct and to the point. If I interrupt, it will be because I think it is not answering the question or I want to move us on. Is that all right?

Lin Homer: That's fine.

Q2 Chair: Good. It might be helpful if I tell you what we are going to cover. We will start with tax avoidance and the tax gap, then move on to RTI, error and fraud, and then PAYE, and I will want to raise bits and bobs with you at the end. Is that all right?

Lin Homer: Yes.

Q3 Chair: That gives you the structure. I will start with the tax gap, Lin. It is £32 billion. Do you include in that the potential income from tax avoidance?

Lin Homer: What we include in our version of the tax gap is money that we have not collected. We do not include the compliance yield that we gain by the work we undertake.

Q4 Chair: On tax avoidance, or evasion. I have not mentioned evasion in that.

Lin Homer: It is the money we think we should have collected, but have not.

Q5 Chair: Money that you know is owing. I know it is a contentious sum. In fact, if you added in the potential tax take from avoidance and evasion, it would be higher.

Lin Homer: Oh no. There have been some very interesting articles about what we think, what Richard Murphy thinks and a very interesting summary of the

two. What we do not include are some of the areas that others include, where they think things should be taxed but they are not under the current law. We do not include money that is not currently collectable—

Q6 Chair: No. I understand that. Tax avoidance is where there is a dispute as to whether it should be collected or should not be collected. But that is not in there?

Lin Homer: If we think it is money we could legally collect, it is in the tax gap.

Q7 Chair: It is in there.

You have written off £5.2 billion in 2011–12, and that is what you call remissions and write-offs. In that, is there any money that you believe you should get from companies that are trading in the UK?

Lin Homer: The £5.2 billion that we have written off is actually made up of £4.2 billion of write-offs and about £1 billion of remissions. Those are sums that we regarded as owing. In the case of the write-offs, where we believe that we are no longer legally able to collect, over 90% of those are insolvencies.

Q8 Chair: Would it include some of these contentious figures around what you think might be collected if the tax avoidance scheme was not there?

Lin Homer: It is very dependent on what you regard in there. What it would include is money that we have said to a business is owing, but the business has gone into administration.

Q9 Chair: So it is a bit unclear.

Lin Homer: It would not include the general sums of money that might be talked about that big business should pay more of.

Q10 Mr Bacon: It wouldn't?

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Lin Homer: Would not.

Q11 Mr Bacon: No, I would not expect it to. Can I be clear about one thing? It is interesting that you said—actually, in a way it is obvious—that 90% of it is insolvency, but where you believe you are legally entitled to the money, it remains an account receivable year after year and does not get written off. Is that correct?

Lin Homer: No, we remit some, and the sums we remit are amounts that we think are unenforceable. Effectively, when we remit, we put those to one side and say that, for value-for-money purposes or the scale of return, we are not going to pursue this.

Q12 Chair: Let me get this clear in my brain—I know it is very complicated this stuff. In a deal you do with the Starbucks, the Googles, the Amazons—I am not expecting you to comment on them individually—would there be anything in your write-offs that reflected the fact that you have not got as much money as you might have thought you would get in the beginning?

Lin Homer: No.

Q13 Chair: No, right.

Can I just say another thing about the tax gap? The tax gap in 2004–05 was £33.3 billion; in 2011–12, according to your annual report, it is £32.2 billion, so that progress is extremely disappointing. Would you agree, and would you like to say why, given that the policy to close the tax gap has been in place since 2006?

Lin Homer: I think the place to start is by saying that the tax gap is a relatively new mechanism for HMRC. Personally I think we are still looking broadly at the trend we are following, and there is a degree of risk in absolutely judging year on year. Overall, we believe the tax gap in the UK is very competitive compared with most countries. It is below that in Sweden and the US, so I would be surprised—

Q14 Chair: But it has not moved.

Lin Homer: It is trending very slowly downwards.

Q15 Chair: I asked for the figures in the NAO, and I got them for 2004–05. We know that in 2006 it became a Government priority to close that tax gap, and one assumes therefore that resources have been, over time, focused on working towards that. Therefore, to see that there is hardly any progress is deeply disappointing.

Lin Homer: I would not agree that it is disappointing, but I think we still have a lot to learn—

Q16 Chair: Why? Why wouldn't you agree?

Lin Homer: Because we have maintained a level of tax gap in this country which is, as I say, among the best in the world. I think that that is down to two things.

Q17 Chair: But you have not reduced it, which was your aim.

Lin Homer: I think it is down to two things. One is that we are maintaining a general level of compliance

in the system which is better than almost anywhere else. The fact that 92% of tax is paid in this country is largely due to the fact that people understand that they should pay and they pay it. The compliance activity that you undertake underpins that voluntary compliance, as well as bringing in the extra.

Q18 Chair: So compliance will never do more than keep you standing still.

Lin Homer: Not never, but some of it is absolutely designed for you not to lose ground, particularly in difficult times—

Chair: I have to say that if we are putting a load of money into compliance, I would expect that gap to come down.

Let me raise another issue with you. In 2004–05 corporation tax was 18% of tax revenue; today it is only 13%. Doesn't that demonstrate your failure to get to grips with tax avoidance in the corporate sector?

Lin Homer: I don't think so. Corporation tax represents about 25% of the tax gap, which is less than—sorry: large businesses account for around 25% of the tax gap, and that includes the sums they owe—

Q19 Chair: Large businesses are 25% of it?

Lin Homer: All taxes paid by large business, so more than their corporation tax—

Q20 Chair: This is your 770 large businesses?

Lin Homer: No—and the 8,000 or so that sit below that. That is less than their share of the tax gap, so they are a smaller proportion. It has been a policy of successive Governments to make the UK an attractive place for business, so there are policy choices that have led to the reduction.

Q21 Chair: You say it is UK Government policy. The figure I was using was that in 2004–05 18% of tax revenue—I am off the tax gap in a way; I am looking at the tax revenue, at the money we get—was from corporation tax, but now, it is only 13%. That suggests to me that we are failing to get to grips with tax avoidance and we are settling for less tax from the corporate sector. The corporate sector has grown since 2004–05, even despite the events of 2008–09 and a double-dip recession. It has grown, yet you are taking more from—dare I say it?—hard-working individuals paying their PAYE than you are from corporations as a proportion of your total tax take. That leaves you needing to answer this question. In a way, you may have answered it. You are saying you are doing that deliberately because Government want to make this an easy place to be.

Lin Homer: I think successive Governments have wanted the UK to be competitive in the global tax system. I think they do want us to strictly enforce the tax laws, and I think we are all recognising that that needs to be underpinned by strong international standards, but you would have to look at the element to which that is policy shift. Corporation tax has been coming down—

Q22 Chair: I have to say to you that that rings with KPMG's advice to its corporate clients that from 2014

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they will have an effective tax rate of 5.5% in the UK. Is that to encourage them to come?

Lin Homer: That's not corporation tax—

Amyas Morse: I am sorry to interrupt you, but if you look at the bottom deck of the table there, it is telling you what the share of corporation tax as a proportion of total tax take is. The percentage you were talking about is the percentage of the tax gap, but these percentages at the bottom line are percentages of tax revenue. Do you see, at the bottom line? You'll need to go over them. I don't think you have this table—

Lin Homer: I don't think we have that.

Amyas Morse: But can you go and do that?

Paul Keane: It is pretty stable for corporation tax. It is 9% in 2004–05.

Lin Homer: I was going to say I think the proportion of the entire tax take is between 8% and 9%, so if the figures you quoted are the proportion of the tax gap, that shows it reducing, which overall shows corporates—

Q23 Chair: Okay, I take that point, but it strikes me that KPMG is saying that the effective tax rate is 5.5%. What have you got to say to that? That is what it is telling its clients: from 2014, come to the UK because your tax rate will be 5.5%.

Lin Homer: I think the Government's position on multinationals is that we do want them to see the UK as competitive. We do expect everybody to pay their fair share. Corporation tax has been coming down, but not to those levels. There are other elements that are properly allowed to be taken into account to reduce the tax yield; that will include losses, but it will also include some investments in certain assets or research.

Q24 Chair: Undoubtedly you have looked at what has been rumbling around the media for weeks—I do not think a day goes by when they do not ring me up about yet another tax avoidance scam that they have uncovered. Do you agree that tax avoidance, particularly by global corporations—if we can look at them a bit—although it may be legal, is wrong?

Lin Homer: Probably most countries are trying to collect their share of the tax that is due to them, and I think it would be fair to say that the Chancellor thinks it is important that he and his colleagues in the OECD environment do what they can together to ensure that big companies are not, in a sense, gaming the system, and so the OECD laws are there to underpin the relationship between countries. What I think is important is that we have very strong rules about transfer pricing; we have put in place very strong rules around CFC; and we believe that we collect the tax owing to us under both our national system and the international system.

Q25 Chair: You are giving a mixed message, Lin. You have to understand that there is a mood of anger and huge frustration out there. Ordinary people and small businesses in all our constituencies feel hassled by you. They feel that if they do not pay their tax, somebody comes very quickly—indeed, you may get an agency to come and get the money from them—whereas big corporations might be invited in to HMRC for a cup of coffee, or your officials might go

have a cup of coffee in the UK head office of the global corporations, but no similar stringent, fair and equal effort is put into ensuring that they pay their fair rate of tax. In your answer, you are saying, “Well, we want them here.” Will you tolerate their paying less tax because you want them here, or will you pursue them equally and fairly as you do other taxpayers, be they individuals or SMEs?

Lin Homer: There are two questions, if I can answer both briefly. I am absolutely clear and want to say without hesitation that we apply the rules fairly across the piece. We pursue the tax that is owing and use a range of methods to pursue. We can have one-to-one relationships with big business, and we do, but we do that in order to make sure they comply. Large business compliance has brought in an increasing amount of money—£3.6 billion in 2005–06, up to £5 billion last year—and transfer pricing brought in an additional £4.7 billion. There is one system, and it applies to all. The second question you asked is about the application of the law. All that HMRC can do and all that you would want us to do is apply the laws. I acknowledge that in an international setting, multinational businesses can choose, to some extent, where some parts of their business are based and where some of their profits are based. As I acknowledged in front of the TSC, I think that that is hard for individuals to understand. It is one reason why the Chancellor and his colleagues want to make sure that OECD stays ahead of that game and does not allow an inappropriate amount of moving-around activity that would undermine the good tax systems of most of the countries involved.

Chair: We want to develop that argument.

Q26 Austin Mitchell: Is tax avoidance increasing? We are told that corporation tax receipts have decreased by £6.3 billion in the last year. That could be partly because of the recession, but it could also be partly because tax avoidance schemes are more commonly used by an increasing number of corporations. Do you have any way of telling us whether those schemes are being used to an increasing extent?

Lin Homer: We believe that big corporations in the UK are getting better at applying the rules, using our disclosure systems and ensuring that the boardroom takes adequate account of taxation issues. We think it is an improving situation. Of course there will always be some—

Q27 Chair: Improving in what sense?

Lin Homer: In the sense that people are complying. They are disclosing their schemes. Indeed, because the tax gap overall is staying stable and reducing slightly, we do not believe that tax avoidance is on the increase. There will always be people offering schemes, and there will always be people using them.

Q28 Austin Mitchell: Yes, but more and more corporations are buying schemes from the big four accountancy houses, aren't they?

Lin Homer: We believe that the big organisations in this country are not utilising what you might regard as the egregious tax systems to a growing extent. We

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feel that we have made significant progress in ensuring that the most senior people in big businesses take tax very seriously.

Q29 Austin Mitchell: But if the Government are saying to big corporations, “Come here, we’ll give you a happy tax regime and possibly dinner with Dave Hartnett,” they are also saying to you, “Go easy on the big boys,” and, ipso facto, “Be tougher with the ones who can’t leave and have to pay their taxes here.” That is the reality, surely. You are handling the big corporations more gently, more delicately, more kindly and more generously than the small and medium-sized enterprises—British companies that cannot shift their affairs through a tax haven.

Lin Homer: No, I do not think we are handling big business gently. I can absolutely refute any suggestion that I have been told to go easy on big business. I have been given £917 million investment to increase yield, and a significant proportion of that comes from big businesses. The figures that I have quoted show the increases we have seen. Our high-risk corporate group has dealt with 1,800 issues and £16 billion since about 2006. We are pursuing all the tax that we think is due. We do it in different ways because it is more effective to persuade people to pay tax when it is due than necessarily to prosecute—I am sure that we will have that debate as well. It goes without saying that you can have a different relationship with 700 big businesses—that can be more one to one—but with big business, small business, big individuals or small individuals, we are making sure that people are paying the taxes that are due.

Q30 Chair: Let us unpick this a bit. You have 770 large businesses and the figure that we had from you last year—I accept that it was a potential figure and not the nth number—was £25 billion outstanding. That was the figure that the NAO had in its Report last year. How many of those 770 large businesses had a parent company outside the UK?

Lin Homer: I am not sure that I can tell you that off the top of my head.

Q31 Chair: Can Mr Troup, who is in charge of this, tell us?

Edward Troup: I am not in charge of large business tax. That is Mr Harra.

Q32 Chair: Well, you have not brought him, so someone must tell me.

Edward Troup: What I can say is that of the £136 billion which those 785 businesses contributed, something like half came from foreign-owned businesses.

Q33 Chair: But how many of the large businesses have a head office outside this country?

Edward Troup: I think that it is slightly less than half, but it might be slightly more.

Q34 Chair: About half, okay. You treat them all fairly, but is it also true that there has not been one litigation against a large business since 2004? Am I

wrong in that? I hope that you are going to tell me that I am.

Lin Homer: When I came to see you before, I gave you a list of some of the firms that we had litigated with. I am very happy to produce that list again.

Q35 Chair: Have you litigated with any of the large list since 2004?

Lin Homer: It did include some very big firms.

Q36 Chair: Since 2004?

Lin Homer: Yes, I think so.

Edward Troup: Yes, definitely.

Q37 Chair: Have you?

Lin Homer: Yes.

Q38 Chair: Can you let us know, because if it is litigation, it is in the public domain?

Edward Troup: I do not have a list of actual dates, but these are all quite recent cases and they include a number of very large companies.

Q39 Chair: Can you tell us who, because that will be in the public domain?

Edward Troup: Yes, examples of big litigation successes include Glaxo, the Upper Tribunal, AXA, the Court of Appeal, Carlsberg, PA Holdings, Pendragon PLC and a number of other cases.

Q40 Chair: Are they in the 770?

Edward Troup: I am pretty sure that most of those will be in the 785, but we can come back to you and give you a detailed list if you want.

Q41 Chair: If you look at transfer pricing, which is one of the issues in contention in relation to those global companies, what is the ballpark figure that you are looking at?

Lin Homer: We brought in £4.7 billion under our new transfer pricing arrangements.

Q42 Chair: What is that figure—is it what you are hoping to collect?

Lin Homer: No, that is what has already been brought in through transfer pricing.

Q43 Chair: How much is outstanding? Did you mean £4.7 billion in one year?

Edward Troup: No, that is a five-year total of cumulative transfer pricing adjustments actually achieved.

Q44 Chair: How much is outstanding? In the same way as we had the £25 billion that is outstanding.

Edward Troup: It will be a proportion of that. I do not have the numbers, but I am sure we can find some.

Q45 Chair: It might be more than that, might it not? It might be less than the 50% you have in.

Lin Homer: The £25 billion will include the negotiation about the value of transfer pricing, because, as you will understand, the concept of transfer pricing is that we challenge the value

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attributed to certain transactions within the global arrangement of the business.

Q46 Austin Mitchell: Can you tell us how many of the big corporations are handling their tax affairs through offshore tax havens?

Lin Homer: No, I can't off the top of my head.

Q47 Austin Mitchell: Why not? If they are handling them through Luxembourg, they will obviously pay a lower rate both of VAT, which is the accusation about Amazon, and of tax. If they handle them through Dublin or through the Cayman Islands, they will pay a lower rate of tax. Why can you not tell us who is handling their tax affairs where?

Lin Homer: There is a definitional issue. We probably could give you broad proportions. Chairman, if I may, I suppose this is the kind of information that we hope we can perhaps start to bring you in our annual report—some generic information—but the description Mr Mitchell just used, in a sense, defines tax havens as places that charge less than the UK. There will be some people who charge more than the UK and they would then include us on that list, so you have to think about what your definition is.

Globally, what Finance Ministers across the OECD would be looking at in the definition of tax haven would be those places with impossibly small amounts. You did not mention it, but Ireland effectively has a lower tax rate than we do. I am not sure that people would regard Ireland as a tax haven or seeking to be competitive, but there are some places around the world where the effective rate of tax is very low, at the bottom end of single figures, and I think the question that Ministers are looking at is what can and should the OECD do about that kind of arrangement. That definition of tax havens is something that Ministers are more focused on.

Q48 Austin Mitchell: Why can't you publish information on the cost of transfer pricing, for instance? Another fiddle lurks in intellectual property, where the intellectual property of making coffee—a caramel macchiato or whatever—is so expensive that they have to pay a tribute to Luxembourg for making coffee in that way. These are fiddles that are open. Why can the scale of losses for each not be published?

Lin Homer: Intellectual property is a real thing. It is important to say that it has a market value: if it did not, there would not be many franchises prepared to pay a sum to some of the intellectual property owners in order to have the intellectual property. There are some interesting debates about whether or when we challenge those kinds of sums under transfer pricing, and how easy it is to price those kinds of things—you know, it is quite difficult to get your base market. One of the things the Comptroller and Auditor General suggested to you in his recent discussion with you was that it might be good to have a conversation with you about some of the international benchmarks in this area, what good practice looks like, and what we could do.

It is an area that we are very interested in. We have traditionally played a very big role in pushing for some of the improvements in OECD rules that then

benefit all compliant businesses, so it is an area we are interested in, but you have to be a little careful about definitions. Whether Luxembourg would see themselves in the same boat as some other places you described might be a contentious discussion with some of our European colleagues.

Q49 Fiona Mactaggart: You started your remarks by mentioning how Britain is, if you like, a country that collects a higher proportion of tax than many similar countries; we have a high level of conformity. I believe that that is partly because we have a sense that paying your tax is a civic duty. That was evidenced by what happened when we had self-assessment and people ended up paying more tax, which was a reflection of the civic duty. I wondered whether you had done any studies into what impact the revelations about companies failing to pay their tax has had on individuals' willingness to pay their tax, and whether you have looked at what the consequences of that are.

Lin Homer: You are absolutely right that you have to maintain broad confidence and credibility in your tax administration to maintain the very high levels of compliance that we have. When we make changes to the law, we challenge ourselves quite a lot on the impact that that will have on behaviours; we have become increasingly thoughtful about impact. I think there is an emerging area about how much the consumer, because of their view as a taxpayer, will change habits. The whole field of corporate social responsibility is itself relatively new, and we are beginning to see some evidence that the opinion of taxpayers is altering the behaviours of firms and individuals, which I think is a helpful thing for HMRC.

That is one of the reasons why we have pushed the debate with big business on having tax in the boardroom. Tax is not something you can just push off to your finance people to do in a corner; the main board needs to think about where a company is positioning itself. As part of that debate, we have very clear discussions with companies about where we see them on our risk profile. When they are complying well with the rules and have good systems, they get less investigative time and attention from us than when they are more risky. We think that is a perfectly proper conversation for us to have with big business. The ones that are at the wrong end of our scale know that very clearly.

It is for Parliament, if I might say so, to determine whether this country wants more of that information to be in the public domain. I know that is a debate we have had over and over, but until the rules are changed, it is not for me—I do not think I have the freedom—to rebalance that myself. The pressure of public opinion may well cause some companies to be more explicit than their annual accounts require them to be about their tax strategy. That is certainly a debate we have with them: what is your tax strategy? Do the people who invest in you and buy from you know what your strategy is?

Q50 Fiona Mactaggart: One thing that I know the Treasury Select Committee regularly raises with you, and I am sure it did last week, is the morale in your

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Department. On this shift to the taxpayer saying, “You guys should be paying your tax,” rather more explicitly than perhaps they previously did, what impact has that had on the people who work in HMRC?

Lin Homer: I think my staff and colleagues welcome the greater interest in tax. It is good, particularly for my front-liners—people who investigate and work with people—to know that it matters to the general public that we have a good and fair system that is complied with. The idea that tax is a topic that is more frequently talked about in the pages of the newspaper, in the pub and around the dinner table is welcomed by staff, and I am encouraging them to continue that debate. One of the things you suggested to us on previous occasions is that perhaps more education early on for young people about paying tax would be good, and certainly our experience is that small businesses that get into good habits with us early on stay in those good habits throughout the longevity of their time as a business. Generally, I think people feel good about the fact that the importance of paying tax is now more recognised and more talked about.

Meg Hillier: I wanted to move on to tax credits.

Chair: Can we come on to tax credits later? I just want to finish this stuff, but I promise we will come to tax credits.

Q51 Austin Mitchell: Is it possible to ban the sale of tax avoidance schemes by the big four accountancy houses? For years, I have urged that auditors be banned from selling other services, such as tax avoidance, to audit clients because I think that weakens the audit. They tried that in the States and a big propaganda campaign by the accountancy houses defeated it, but, theoretically, would it be possible?

Lin Homer: That might be a question I throw to Edward, but I would start by saying that the requirement to disclose is quite punishing. Of course, you will remember in the last year that we have seen the Chancellor move to use retrospective action in the case of a disclosure.

I am sorry to say this again, but one of the challenges for us is definitional. Tax planning is a good thing that we encourage people to do, and egregious tax avoidance is something that we know we do not want. The gap between the two is the area where disclosure is important.

What we are doing now is very rapidly moving to make public our view about emerging schemes. You will remember that on the last occasion I was here, we shared with you what I think we call “Spotlights”, which is our list of tax schemes that we say we do not think will necessarily work. Of course, one of the best ways of stopping this kind of behaviour is for people to stop buying them. There is a basic rule: if it looks too good to be true, it probably is. It is important for customers to exercise some discretion, as well as the promulgators of the schemes.

Q52 Chair: I think we are going to have a whole sitting on this before Christmas.

Lin Homer: We had a sitting on the 6th, when we were expecting to bring Jim Harra, as well as Edward.

We were rather thinking that we would spend quite a long time on this topic.

Amyas Morse: We have a Report coming out.

Q53 Austin Mitchell: I think Ernst and Young has been prosecuted for selling schemes in the States. My other question was: why can we not have—or would it be effective to have, as the Australians do—a general avoidance rule, so that any scheme that is meant to avoid taxes can be struck down?

Edward Troup: We are in the process of introducing a general anti-abuse rule, which will be published in draft on 11 December and be up for consideration in the Finance Bill in four or five months’ time. So the answer is yes.

Austin Mitchell: Thank you.

Q54 Chair: I want to ask a few more questions, then we will move to Meg and the tax credits. Let me ask this general question first. In your initial answer, Lin, you talked about the balance between encouraging companies to come here and pursuing them for tax. Where is your priority? I want to get a sense of where the priority lies. You cannot do both, so what is the priority?

Lin Homer: For HMRC, the priority is to collect the taxes due. So we have a role in making sure that the tax system is as clear and understandable as possible, so that people will comply with it; in making sure that the system of collecting tax works—and we have seen the challenges, such as the introduction of NPS, when we do not always get that right first time; and in pursuing through compliance those people who, through error, fraud or criminal activity, try to stay out of the system. Our priority is to get in the tax due. For the Government, there is a balance to be struck between having a competitive tax system—

Q55 Chair: So you do you get told, “Don’t pursue too hard”?

Lin Homer: No, we do not get told, “Don’t pursue”; we get told, “Pursue rigorously, to the laws”.

Q56 Chair: Okay. If you are told to pursue rigorously, let me do some examples. If you take the Lagarde list that has been in the press recently, HMRC said, as quoted in *The Times*—no doubt, you will tell me, in error—“The courts would not thank HMRC for taking zillions of prosecutions into them, so we have a selective prosecution policy”.

All I would say to you is that this is tax evasion, but there would be a public outcry if it was someone selling cars or something, or fiddling car sales, and you decided to have a selective prosecution system. Why have a selective prosecution system on tax? If you have a car theft cartel, you would prosecute. Why, if you have got a tax avoidance or evasion cartel, are you selective in who you prosecute?

Lin Homer: I think it was the occasion I attended with Mike Eland. We talked at length about the need to have a complete range of approaches—

Q57 Chair: But why “selective”? Is it true? You are quoted—you have a selective prosecution policy.

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Lin Homer: I will ask Edward to update you on progress with that project overall, but we have always taken the view that the important thing is to get the money in and to persuade people to pay the tax due. We have well published approaches that say that we will tend not to penalise even, let alone prosecute, people who come to us and voluntarily disclose; people we have to work harder with, we will penalise, and we will take that all the way through to prosecution. So we have always taken a view that we have to have the whole toolkit, but on these particular cases we think we are having some success.

Q58 Chair: You have one prosecution.

Edward Troup: Yes. May I put some of the facts on the record? The figure of 6,000 has been bandied around as the total number of names, but that is the total number of entities, which is quite important because it includes companies, trusts and other entities; it is five-year-old data so it has taken a bit of time to work out who are the individuals in the UK whose names are on the list.

It is only a list—it is intelligence, not evidence. We have had to turn that into evidence that the individuals—some of whom have quite legitimately got the money there—have actually underpaid tax. Having said that, we are making very good progress. Criminal prosecutions always take longer, because of the additional burden of proof.

Q59 Chair: You have got one at the moment.

Edward Troup: We have had one so far. We have got another dozen criminal ones in train.

Q60 Chair: Another dozen?

Edward Troup: Another dozen criminal ones in train, which is roughly equivalent to the proportion of criminal to civil that we generally find, using the criminal investigations policy, which is published, which explains how we will always use civil fraud measures before we come to criminal prosecution. We have got 500 who actually we have settled with, and got money; we have got another 200 who have voluntarily fessed up; and we have got another 400 who have used the Liechtenstein disclosure facility. So we have already got 1,000.

We have got over £120 million of cash in, which I think is more, actually, than we had anticipated. The number is still rising, and we do expect to get out quite soon—to initiate, and engage with the remaining individuals who are represented in this list. So actually we have got a very good story to tell on this, and the selective choice of one prosecution out of 6,000 is, indeed, selective. We are actually quite proud of what we have done on this, and it is part of the wider offshore evasion strategy, which is bringing in, as you know, very considerable amounts of money.

Q61 Chair: Can I ask you about another one? I know you won't want to talk about Starbucks individually, but one of the interesting things with Starbucks is they appear to have structured—we will find out next week—their business in such a way that there is no profit here, both in terms of what they pay for loans and in terms of the royalties. Now, do your

investigations go into trying to understand the profit structure of a company, or do they just stop at the border?

Lin Homer: No, no. With our multinationals we have a range of opportunities not only to see the detail of their arrangements but to challenge it, so transfer pricing—

Q62 Chair: So you look beyond what they say they do in the UK? You look to the States—you look at all their other businesses, do you?

Lin Homer: Yes.

Q63 Chair: So how many of your staff are currently doing Starbucks, for example—or any of them?

Lin Homer: Well, you know we won't talk about that.

Q64 Chair: I know, I know. So you have got 770 big businesses. Tell me how many staff you have got looking after the 770 big businesses.

Lin Homer: Well, we have a range of people.

Q65 Chair: How many staff?

Lin Homer: Large business, which is part of business tax—

Edward Troup: The large business service has 1,200; large and complex, who deal with the other large ones, have got 1,700; and that nearly 3,000 draws on experts across the department. So for instance we have 65 transfer pricing experts. So this is a well resourced unit, which is bringing in very significant amounts of money.

Lin Homer: And we do work very closely with colleagues. You have mentioned the US, but this is not an approach which is done in isolation. As I say, we know and understand that the Chancellor is very keen to continue that co-operation and to continue to work with other countries to ensure that we do stay on top of these approaches and get the best—

Q66 Chair: I am not sure we would say you are on top of them; that is the problem. If you look at all of them—don't only take one, but look at all of them in there—and look at their turnover and profits, as reported quite often in the States, on their UK business, their tax in relation to either the turnover or the profits reported in the stock exchange commission in the United States does not bear any relationship whatever to the corporation tax they pay here. So I don't feel you are on top of it, Lin.

Lin Homer: We are applying the rules of the game as they are at the moment.

Q67 Chair: Are you?

Lin Homer: Yes, we are.

Q68 Chair: It is very difficult, because I am trying not to take individual circumstances, but if you take a company that claims it has to pay 6% in royalties, that doesn't even look competitive, because at the end of the day it then puts into UK Companies House that it is making a loss. It does not seem to me that you are getting underneath that at all, and this is a company giving another wholly-owned subsidiary the entire 6%—plus, then, the loans and everything else. You are

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not getting underneath it, and it doesn't reflect their business or the cups of coffee they sell in the UK.

Lin Homer: We won't talk about individual companies. It may be that you will invite them before you, and some of them will be more willing to talk about their strategy. What I can assure you is that we are confident that we are getting what we should out of the current system and that we, and Ministers, will continue to be alert to the possibilities to improve the system. Really, as I answered to Mr Mitchell, I think a number of us would accept that in a system where there is some choice about where you base yourself, and some of those choices are very, very small tax rates—

Q69 Chair: But you are not getting anything. You look at these big businesses doing big business in the UK and your corporation tax take varies from zero, 2%, 3% or 4%. It's all down in the nothings. You can't say, "We're doing it properly." Without taking any individual case, you can look across the whole range of them and you cannot then tell us that that reflects a fair corporation tax credit to the UK Treasury from the business they transact here and the profits they make, as shown in their American accounts. You can't say that.

Lin Homer: Multinationals are subject to global tax rules. We are part of the process which can develop and challenge those rules, and I think it's right that we should be. I am confident that we ensure the application of those rules, to ensure that the UK is not disbenefited by the proper application of the rules. Whether those rules should be changed is—

Q70 Chair: What is wrong with the transfer pricing rule at the moment? What's wrong?

Lin Homer: I think the transfer pricing rules work well.

Q71 Chair: They can't do.

Lin Homer: I think they do, and I think—

Q72 Chair: So you think it's fair that all these companies can take so much of their profits out and put them into jurisdictions where they pay no tax by using transfer pricing?

Lin Homer: That is not the question you asked me. I think that the transfer pricing rules work well within the framework that they're based in. And I think that you have to remember that intellectual property has a real value, and there will be British firms that will benefit from this kind of approach themselves. So the basic rule—

Q73 Chair: They put it in another tax haven somewhere else, do they?

Lin Homer: No, but they will charge people for their intellectual property. And so you just have to—

Q74 Chair: But they won't pay tax here.

Lin Homer: Well, this was a point I made to Mr Mitchell—that I think many people, including probably quite a lot of Finance Ministers throughout the world, would think that a situation where some countries offer very, very low tax rates is a challenge

for all of us. That is different than saying that I have reservations about how we apply our expertise to the rules as they are currently drawn, and I am confident that we do that well. I think we're regarded as leading in this field, and I believe it's one of the reasons why the work of the business tax directorate does bear scrutiny and does work well for the country. It doesn't mean that we wouldn't want to see some of those rules changed.

Q75 Chair: So Charles Elphicke's work, which showed a corporation tax rate of 3% on the 19 global companies that he looked at—was that a load of rubbish?

Lin Homer: All I would say is that you can't always tell as much as you think from the published accounts. It's something that a number of my people have said here and in front of the Treasury Committee—that the information that organisations are obliged to put in their published accounts is not always—

Q76 Chair: We ought to know what tax they've paid. We may not know about the negotiation, but the tax they pay is eventually shown in their published accounts. So I assume that his figure of a 3% corporation tax rate is correct. I wouldn't think he's made that up; he is a tax lawyer by background.

Lin Homer: I think he's drawing on what he knows. My point is that not everyone—

Q77 Chair: You can't get away with that, you know. Either—

Q78 Mr Bacon: Can I come in here? People understand—at least, they'll understand if they think about it—that if you run a shop in the Dubai airport called Laura Ashley and it's a franchise, you will have to pay a fee, an intellectual property fee, to the owners of the Laura Ashley company, in order to do that, and you will have to abide by certain standards and rules, and design guides and the products you sell, and all the rest of it. There is a huge advantage in being Laura Ashley, because when people go through the airport they recognise it instantly. One understands that; the name obviously has some value.

What people don't understand is this. You can have a large business—let us say a coffee chain, for the sake of argument—and it sells coffee. People understand, roughly, what it costs to make a cup of coffee, and the more they study it the more they would understand. And they understand what sandwiches cost, they understand what it costs to rent premises and they understand what it costs to hire people. And you have a set of underlying activity going along, across hundreds of branches. At the end of all that underlying activity, somehow—apart from the income tax and the national insurance that the employees pay—through a set of what are apparently tricks, the corporation tax from that vast array of underlying activity is miraculously reduced to nearly zero. The best that you can say is, "Well, our transfer pricing works pretty well."

It just smells, and not of coffee. It smells bad. You keep on saying, "Well, the rules are the way they are", but you know perfectly well that you and other similar

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tax authorities essentially determine what the rules are and that when you don't like them, you change them. In this country, you put them through Parliament—I have sat on a Finance Bill—and they come out, largely, exactly the way you want them to, and you have been at it for years.

Why is there still this enormous artificial construction that bears hardly any relation to what most people would understand as a sensible set of economic arrangements, with some relationship between the underlying economic activity of the company and the amount of corporation tax paid? There is this enormous gap, and the biggest gap is in your credibility. That is why it is a huge public issue. People do not understand it.

Lin Homer: I am trying to answer.

Q79 Mr Bacon: I'm sorry that I'm not letting you answer, but you must understand that the reason why people don't understand is that for years you have done a really bad job of explaining.

Lin Homer: Well, I disagree with that comment.

Q80 Mr Bacon: Then why don't they understand?

Lin Homer: If you will let me just have a quick go at answering the question—I said to the Treasury Select Committee that I can understand people's reaction to some of the descriptions of behaviours that they will see as smelly—not a nice smell—as you just described. You don't necessarily know all of the ins and outs of the business from the published information. Let me give you an example that is not in the coffee arena, but then I will return to that. We have, for a number of years, heavily encouraged scientific entrepreneurs. We have tax approaches that are designed to allow quite significant recognition of the investment costs up front for stonkingly good new developments. We then developed some very successful businesses that make a global impact, because of the quality of their—

Mr Jackson: I'm going to stop you there. I may not be the brightest sparkler in the fireworks box, but I think it is incumbent upon you to distinguish the intellectual property rights of picking a coffee bean and roasting it from Pfizer developing a world-beating drug in Sandwich or the US.

Q81 Mr Bacon: If I may agree with Mr Jackson's interruption, my point to you was that you had done a really bad job of explaining and you said, "No, I disagree" and started talking about something completely different, which is high-end science. We are talking about coffee and sandwiches. That is not high-end. My whole point was that it is simple: you rent premises, you hire some people, you make some coffee and sandwiches, and you sell them. It is not that difficult. If you are trying to explain that by reference to high-end science and the tax breaks available for high-end science, I will make my point, which I know you disagreed with, again: you are not doing a very good job of explaining it. Explain it in terms that people understand—coffee and sandwiches and the things that people can understand.

Lin Homer: I will have another go. I apologise—I did not hear you say "explain". I thought that you were

talking about our activity over the past few years. I am perfectly prepared to accept that I did not persuade you with that explanation.

Q82 Mr Bacon: I don't just mean me; the public out there don't understand it.

Lin Homer: I understand. I was trying to give an example to the broader question that had been put to me that you—

Chair: Just focus on that.

Mr Bacon: Not by me. My question was not a broader question.

Lin Homer: One of the interesting challenges, which I think it is reasonable to ask yourself, is that if the intellectual property we are talking about in the kind of areas we are talking about—sandwiches, coffee and produce of that sort—were worthless, people would not pay for it. It is a market-led value that is attributed to this area.

Q83 Chair: This is nothing to do with tax.

Lin Homer: It is.

Chair: What we see is turnover, profits and then tax. They bear no relation to coffee and sandwiches.

Lin Homer: To finish, many of the examples of the businesses that you are looking at have a fairly high proportion of franchises. In those cases, the franchise is paying an amount to the owner of the intellectual property. They are choosing to do that. They clearly think that that is commercially worth while. That is my point about—

Q84 Chair: You cannot say that.

Lin Homer: Yes, I can.

Mr Bacon: She can and she just did, but what you are saying is that they are choosing to hold a Starbucks—

Q85 Chair: Richard, it is different because KFC and McDonalds are similar businesses to the one that we are not allowed to talk about. KFC and McDonalds all pay a little bit of tax in the UK. The one we are not allowed to talk about does not. You have told me the transfer pricing stuff is quite fine, but what none of us can get is why UK tax authorities cannot get underneath the business that is being done, so that the cups of coffee and the sandwiches that are bought in the UK have proper taxes paid on them.

Lin Homer: I was explaining intellectual property. There can be other reasons why one organisation makes more money than another. That can be because of how they choose to run their business, how much they invest in property or how much they invest in training. So, my point is that you cannot tell, in one fell swoop, that intellectual property is—

Q86 Chair: But do you look, for example, with the company we are not allowed to mention, at what they have been telling their shareholders about the profit rate in the UK? I think one of the things they told their shareholders about was the 15% profit rate in the UK, yet they pay no tax.

Lin Homer: One of the values of having customer relationship managers is we get to know these businesses quite well.

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Q87 Chair: Well then, either the skills of your individuals are not good enough or you are not getting underneath things.

Lin Homer: I don't think that is necessarily the only outcome.

Q88 Mr Jackson: But surely there is a difference—again, I come back to my original point—between brand value, which we are talking about with this company, and intellectual property, which involves masses of research and investment over many years, and which is a different issue. My point, building on what Mr Bacon says, is that, surely, the tax authorities can distinguish between the two, because they are not the same. You use this caveat of intellectual property as a catch-all term to give carte blanche, it seems, to admittedly legal and, for the moment, legitimate tax avoidance. But surely it must have crossed your mind that we need to establish some kind of legal precedent to distinguish between brand value and intellectual property.

Lin Homer: The second thing Mr Bacon said in what was quite a long question, which I have not done justice to, was that it is quite easy: you just make a national law. That is also not true because—

Q89 Mr Bacon: Actually, if I did, I didn't mean to, because it needs to be done internationally. The Committee met some Harvard tax experts recently—

Lin Homer: It does have to be done internationally, and intellectual property is defined internationally. This is not something in which we can, if we want our own companies to benefit from consistent laws, just make up our own versions. Intellectual property covers quite a wide range of things.

Q90 Mr Bacon: When you have a business model that is so relatively simple in terms of what it does and the service it provides that it is easy for most people to understand, and which operates on a large scale and at a high level of economic activity, and yet pays no corporation tax, the only conclusion people can really come to, whether the situation has arisen because of payments for a franchise or payments to service debt, or because interest rates are very low, is that the business pays no corporation tax because it has—people are going to hate this verb—architected things that way so that it ends up paying no corporation tax. The Chair talked about other companies, and perhaps they just have poorer tax advisers. It beggars belief that such a large entity, with so much underlying activity here, can pay so little corporation tax. That goes back to the question of your transfer pricing and—Mr Troup said you have plenty of experts—whether you are really getting underneath things. These things do not seem credible to the vast majority of the public, which takes me back to where I started: this has not been explained satisfactorily.

Lin Homer: I hesitate to go back, but we are in a position where, by law, we are not able to put an individual example on the table and unpack it for you. As I said earlier, it is open to individual companies to say more about their own affairs. Their decision about how much they speak or don't speak is a matter for

them and for corporate policy. As you said earlier, we have seen some individuals prepared to go on record and make statements.

Q91 Chair: We are delighted they are giving evidence to us, but before this becomes about individuals, what has been in the papers? I probably haven't picked it all up. Amazon, Starbucks, Google, Apple, Asda, Facebook, eBay, IKEA, Intel, Kraft, Coca-Cola—this is not an individual company; this is a generic problem.

Lin Homer: And multinationals have choices. Multinational companies are companies which can choose where to put their headquarters and where to put their outlets, and they are taxed in the country where they carry on economic activity, not where their customers are. That is an international arrangement.

Q92 Chair: Hang on. They are taxed in the country where they carry on economic activity.

Lin Homer: It generates their profits.

Q93 Chair: So we have Kraft, Coca-Cola, Amazon, Starbucks, IKEA and Asda. All their economic activity is clearly in the UK.

Mr Bacon: You make it sound like customers are not part of economic activity. In fact you did; you just said that.

Austin Mitchell: They have their biggest sales in the Channel Islands, presumably.

Lin Homer: Not all economic activity is related to the final element of the sale and transfer. I would simply make the statement that all the companies that benefit from this, benefit from it. In a sense, we are complying with international approaches, which apply to our companies as well, and we think we apply those rules well.

Q94 Austin Mitchell: Talking about transfer pricing, I am just reminded of a thing I unearthed with Prem Sikka in one of the pamphlets we were writing. I wish I had swotted it up before I came. On transfer pricing, one firm was charging its subsidiaries in, I think, this country, \$3,000 for plastic lavatory seats, and it got away with it. We drew this to the attention of HMRC and nothing happened. But that's just a thought.

How much of this problem is down to the fact that you are not well resourced enough, or smart enough, to deal with it? I remember what Bob Sheldon said to me when I was appointed—early days; a long time ago—to the Finance Bill Committee and had the pleasure of sitting up all night. He was introducing legislation to stop a certain tax avoidance scheme and he said wearily, in the late hours of the night, that it was all very well, that this would stop it, but that “these big accountancy houses employ some of the best brains on the highest pay in the country and we can't keep up with them. They'll be back with another, even better scheme within weeks.”

Lin Homer: I think we are smart enough. If you would like us to, Edward could talk you through some of the work we are undertaking through our tax academy to make sure that we not only recruit the best but train them well and keep them well.

Chair: We welcome that.

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Lin Homer: Fortunately for us, not everyone is turned on by high salaries—

Q95 Austin Mitchell: But have you got the staff and the quality, ability and brains to cope?

Lin Homer: We keep many people for the whole of their career and we keep another significant proportion for a large part of their career, and what I will say is that they are often made offers by firms, which they resist. I think that some people are still very motivated by the public service ethos.

We are part way through the reinvestment programme, and a proportion of that has gone into business tax. Again, when Jim is with us at the next hearing, we can talk about what we are doing with that. I personally feel that if I got to the point where I felt we could do more in business tax with more people, I could go back and ask for more.

My view is that we have the right talent. It is helpful to us to have an increasingly large public interest in this, as I said earlier. People should feel that paying tax is something that is expected in this country. Overall we have a good story to tell.

Q96 Austin Mitchell: It would be interesting to know how many gamekeepers turned poachers over the years. I have one other question. How is it that the big four accountancy houses, which are devising all these clever schemes and flogging them on to firms to avoid tax obligations, are also advising the Treasury and HMRC on bringing in more taxes and improving the tax system? How can they do that job at two ends?

Lin Homer: I think that all Governments have tended to ensure that they consult. We do not listen to experts from other fields with an entirely disingenuous view. We challenge other people's views.

Q97 Austin Mitchell: But you trust them.

Lin Homer: I think that the tax sector is populated, in the main, by very professional, very able people. The Treasury Committee had some of the tax agents in the week before we appeared, and I think that if you asked the Committee it would say that some of those people are helping us to make the tax system better.

Yes, I do trust them. That is not to say that there aren't some charlatans in the world selling schemes that are designed to part people from the money or part the country from the tax it is due, but I believe that we are good at finding them and good at closing them down, and when the Government need to they are prepared to legislate retrospectively.

Q98 Fiona Mactaggart: One of the things that you have been saying is that you target your activity according to the behaviour of the company. Yet the NAO Report, at paragraph 3.18 and 3.19, implies that the analytics approach and taxpayer profiling that this Committee demanded in its last two Reports, in 2004 and 2009, is only just coming into force. I am wondering when we can expect you fully to implement that plan of approach?

Lin Homer: That was such a short question, I was not expecting the end of it.

Q99 Fiona Mactaggart: I don't want to deliver an essay; I want you to deliver it.

Lin Homer: I think the references in paragraphs 3.18 and 3.19 are particularly about some of our work on debt. We have talked to you before about some of our new investment in technology that gives us much more powerful data analytical tools. We have also talked to you about the fact that we know we are not getting full power out of those. I suspect the reality is that, by the time we have got full value out of Connect, which is one of our most powerful recent introductions, there will be another powerful system just round the corner that will take us even further. We are now doing things that we would not have been able to do even five years ago, and the cleaning up of our systems and getting them to talk to each other is allowing us to make greater use of them.

Only a few years ago, HMRC had more than 3,000 systems, so with the best will in the world, even if you had data analytics, it couldn't Hoover up from all the systems. Now, we are increasingly moving towards having a "big 13" systems, through which you can put your analytics and get much more comparison. I think it will enable us to chase debt, to challenge people and to target resources, but I am pretty sure that once we make the best use of those, someone will have an even more powerful machine for us to think about investing in.

Q100 Fiona Mactaggart: Will it enable you to challenge people doing similar kinds of business but—this is the point that Mr Bacon was making—treating their payments back to head office in a quite different way?

Edward Troup: We've started the customer segmentation model with the large businesses, because the large business working-with-business programme was about putting them into high, medium and low risk on a number of different factors, and in a sense the numbers are in front of you. Giving a low-risk rating to businesses that we can see are compliant and are not using aggressive schemes, and putting more resources into businesses that are high risk and are more aggressive, for whatever reason, such as their location, or the nature of the schemes, has produced the sort of results that you have seen. The high-risk corporate programme since 2006 has dealt with 1,800 issues, and collected £16 billion in extra revenue. That is customer segmentation. It was right to start at the largest end with large businesses: they pay the vast proportion—60% of overall revenue comes through them. Rolling that out across the whole customer base and trying to adopt the same approach is work in progress.

Q101 Fiona Mactaggart: So you don't know when you will have it rolled out.

Lin Homer: I think we are already getting incredibly good value out of the system.

Q102 Chair: Right. I want to ask you three quick questions, and then we will go on to RTI. First, you say in your report that you use debt collection agencies.

Lin Homer: Yes, we do.

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Q103 Chair: Do they pursue large businesses as well? Have you got a debt collection agency pursuing large businesses?

Lin Homer: The debt collection agencies have so far been used to pursue the small debts that we would otherwise not have pursued ourselves.

Q104 Chair: Why? Is it a matter of a cosy chat over a cup of coffee, or you have the bailiffs in?

Lin Homer: No. We have skilful internal debt collection approaches. We found, as we discussed with you at earlier hearings, that because we always tend to put the investment where the returns are higher—in the top-end debts—we were not pursuing some of the smaller debts at all, and we were beginning to see small debts where people were clearly working out what they thought was the level below which we wouldn't go. The debt collection agencies are very much at the bottom end.

Q105 Chair: Okay. I get that, but can you tell us, or will you write to us, about how many cases you do not pursue through debt collection agencies, but you may pursue through the courts? You do not know how many cases you have against the top businesses at the moment, do you? You talked about some of your successes, but you have not got a list.

Lin Homer: The 1,800 cases that Edward referred to were all cases where—

Q106 Chair: No, in litigation—in courts.

Edward Troup: Litigation with large businesses is not about collecting tax that is due; it is about settling the question of whether they owe us the tax. That is why we take—

Q107 Chair: How many of those are in the courts at the moment?

Edward Troup: I can come back to you. There are about 8,000 items of civil litigation being processed within HMRC at the moment, across the whole range of tax—

Q108 Chair: I am trying to get on to the other thing, but the other thing was the story in the BBC over the weekend about umbrella companies who pay their temporary workers' salaries offshore to avoid NICs and PAYE. Is that legal?

Lin Homer: This is an aspect of the discussion we had with you when you had Nick Macpherson, myself and William Hague here. As we discussed then, there can be legal reasons why you have service companies. They are not necessarily designed to avoid tax, but we will always tend to review and check as to whether what is being put in place is right.

Q109 Chair: How can it be legal? The example was given—I have no idea what the company was—of a company dealing with teachers. I have also been told that construction, engineering and IT tend to use these umbrella companies to avoid NICs and PAYE.

Lin Homer: This is fairly similar to the personal service company. If it is a genuine arrangement and it is offshore and—

Q110 Chair: What would be genuine? If you are working here in the UK, what would be genuine about not paying NICs and PAYE here in the UK?

Lin Homer: It is exactly the same approach that we told you we would use with personal service companies: we would investigate if it is an artificial manipulation of the rule. Whether or not it is set up in that way, we would pursue—

Q111 Chair: If you are working here in the UK as a teacher, IT specialist or engineer—as whatever—or in the construction industry, is it ever genuine not to pay PAYE and NICs?

Lin Homer: It can be in certain circumstances.

Q112 Chair: Like? Give me an example.

Edward Troup: If a French company which specialised in providing specialist engineers made an engineer available to a UK business, and the French company had no place of business in the UK, it would not have to operate PAYE and NICs and the engineer would be responsible for his or her own—

Q113 Chair: But a teacher in a classroom?

Edward Troup: It seems unlikely that the same situation would arise with a teacher, but it is perfectly possible in a specialised teaching area. But we are looking closely at the arrangements and we think that the majority of these arrangements do not work.

Q114 Chair: Don't comply.

Edward Troup: Don't comply. That is what we believe and we will pursue them.

Lin Homer: We will pursue them.

Q115 Chair: Who do you pursue in that instance?

Lin Homer: We may pursue the individual for tax owing, or we may pursue the company that has hired. Again, as we discussed with you when we sat here, I think I committed fairly rashly to a ten-fold increase in the number of interventions, and we are on target to do that. So we will make a judgment about where we pursue.

Chair: Okay. The very final thing is this. The Chancellor has said, "We will be as tough on the richest who evade tax as those who cheat on benefits." Do you think you are?

Lin Homer: I think we are applying our rules across the piece. One thing that I was going to say when we talked earlier about how we apply penalties, we have sheets that tell people how we will respond. They are not just aimed at big or small; they are for everyone, and they clearly set out, with a classic RAG rating, that if you come and tell us you have forgotten to pay some tax, we will genuinely be quite supportive and help you get on your feet; and if we have to work really hard, we will pursue with ever-increasing penalties. So our message is that we expect people to pay their tax and we will be even-handed about pursuing those that do not.

Q116 Chair: Thank you. Let us move on to RTI. We are all worried about this, and no doubt you are too. What is the rating that you have got from the Major

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Projects Authority on your part of this project? What is your rating: red, amber or green?

Lin Homer: I think we were amber.

Q117 Chair: You are amber.

Lin Homer: We are being looked at, I think quarterly, by both the NAO and the MPA, and I think that is helpful¹. It is a big, important project and it is very useful to us. The most recent one was amber, which is sort of where we would expect to be at the moment, with—

Q118 Chair: Six months before.

Lin Homer: But a lot of work to do still. The project has learned something from previous projects. We have approached this by building up from small pilots, but we are trying to stay open-minded to the views of committees, agents, employers about the things that we still need to think about before next year.

Q119 Chair: Okay. We had Nick Macpherson in front of us the week before last, and when we asked him about whether the Treasury wanted to drop the whole thing, there was a very long pause.

Lin Homer: There is often a very long pause before Nick replies though, isn't there?

Mr Bacon: Not that long.

Q120 Chair: He then went on about the chaos, which I recall, with the introduction of tax credits.

Lin Homer: Did he?

Q121 Chair: How do you respond to that—your preparedness on this in comparison with that?

Lin Homer: As I said, one of the important things for HMRC is to learn from its experiences. If you are going to do lots of big projects, at least you can make sure you learn from them.

It is important to remember that we are going through a fairly major transformation of PAYE, and that it needed it. It was a system brought in in the 1940s, and it had had very little done to it. I know that the introduction of NPS brought all sorts of challenges and problems for people, but something needed to happen. A system designed when most people had a job for life was not keeping pace. For HMRC—put to one side what the DWP wants—increasingly to have information come through regularly in real time, will really allow us to run, we believe, a very effective tax system.

It will be useful to us. A lot of the employers who have been pilots with us in this first stage have been really pleased and surprised by how reasonable it has been to enter the scheme and how well the scheme has worked. Of course, though, the real test is as we stand up from a few thousand employers to many thousands. We are not at all complacent, but the reaction from employers has given us heart. Most of

them are finding it is helping them put better data into the system.

There are big challenges. I think we had at least 40 people in the old PAYE system who were supposedly 200 years old—the date of birth they were registered with was that silly. One of the big changes for us is that this is requiring employers to give us better data and then for tax judgments to be made on better, clean data. That will be painful as we go through it, but I think it will give us a very good system in due course.

Q122 Mr Jackson: This is about big projects. I heard you waxing lyrical on Radio 4 about the child benefit changes and the millions of letters you are sending out to higher rate taxpayers. I asked a question of the permanent secretary at the Treasury a couple of weeks ago. Do you repudiate the report in *The Daily Telegraph* about 10 days ago—it prayed in aid the Institute of Chartered Accountants in England and Wales—that you are not ready in terms of your infrastructure to bring in that very significant change? That is the first, quite simple question. The other is: how are you going to cope with some of the very large number of exceptions that you are going to have in dealing with that change? Essentially, are you confident that you can carry through that very major change in tax policy within the time scale without an enormous cock-up?

Lin Homer: The most dramatic descriptions of failure that I have seen in the media, I would repudiate. I think we are exactly where we expected to be in terms of the development of the scheme. We actually have more employers already in the scheme than we expected at this stage, and that has largely been because they have come and asked us to join the pilot, rather than we had gone out looking for them.

ICAEW have raised some important issues that we need to discuss with them. In fact, I was meeting them this morning and was absolutely assuring them that we want to continue working on the things that they are worried about. One of the things they are very worried about is small and micro-businesses, and it is essential that we spend enough time looking at those. A comment I made to one of your colleagues on the Treasury Select Committee was that, to some extent, the challenge for us is that if a small business is running in a fairly chaotic way, it is not the introduction of RTI that is a problem for them; it is that they are running in a chaotic way. None the less, we still have to help them bridge into somewhere where their arrangements can more easily lock into a more regular system. We are providing some free software for small employers; we are looking at what kind of exceptions you need to make—agricultural businesses, pubs and things like that—

Q123 Mr Jackson: Are you on RTI? I am talking about child benefit.

Lin Homer: Sorry, I do apologise. On child benefit, yes, I am reasonably comfortable that quite a lot of the issues that have been written in the paper about that are being over-dramatised. It is a big change for people, and I do not make any comment about that, but if people go on to our website, look at the drop-down questions and put in their own facts, it is

¹ Note by witness: The team meet regularly with the NAO to support their wider audit work on HMRC and the NAO's review on RTI progress will be included on their annual C&AG statement. However, we do not report to the NAO quarterly specifically on RTI. We do make quarterly submissions to MPA to support their roughly 6 monthly Project Assessment Reviews (PAR).

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designed to help them decide whether they want to keep claiming child benefit. If they do not, it is a relatively easy decision to opt out; if they do, they do nothing for now and keep receiving child benefit, but if one parent earns more than £50,000, they have to ensure before next October that they are in the self-assessment system—half of them already are—and they have to fill in the self-assessment. I think it is old-fashioned to suggest that our self-assessment system is beyond the wit of most people.

Q124 Mr Jackson: No, but whether I agree with it or not—I think it is a crazy policy that I disagree with, and I voted against it—you did have a fairly simple system, enunciated by the Chancellor in October 2010 at the Tory party conference, and then, last year, you were told, “Forget all that. Because of the fuss, we have to get rid of the cliff edge, so we’ll do the tapering.” Therefore, in terms of your planning, I imagine the time scale has been quite difficult. That is my concern, and I guess the ICAEW is also concerned about it.

Lin Homer: It has been an important and challenging piece of work, of course, but I think the most important thing for individual families is to go on the website and make a choice about whether they will keep having child benefit. If they will, they have months and months to get into the SA system. Last year we had 800,000 more people do SA than the year before, so the possibility that another 200,000 to 300,000 will have to do so because of child benefit will not overwhelm our system. I am confident of that. I think the biggest challenge is those people in the £50,000 to £60,000 range, where the taper has been provided, because it is really important that they go on and use our calculator to work out whether they will be better off. For most people in that group, if they get their income right, it would be better to take the child benefit and repay some of it, because they will always get more benefit than they give back. One of my concerns is to ensure that people are using the website and the calculator to make a good choice, but I am confident that our website is easy to use—it had had 70,000 hits by Saturday, and people probably had not received their letters by then—and the call centres are ready and waiting for those people who find that they need extra advice after they have used the website. We would really like people to try the drop-down questions first, obviously.

Q125 Mr Bacon: May I return to the question about real-time? When you misunderstood Mr Jackson, you were in the middle of saying—I am interested in this—that there will be exemptions for agricultural businesses and small businesses. Will you repeat what you were saying?

Lin Homer: I think we call them easements, which is a beautifully old-fashioned word, isn’t it?

Mr Bacon: Positively Anglo-Saxon.

Lin Homer: What we are trying to recognise is that there is a very limited number of cases where the nature of the business is such that we really wouldn’t expect people to literally hand over the cash and then type something into the machine straight away.

Q126 Mr Bacon: Because they are too small?

Lin Homer: No, because the nature of the business is day-by-day. For example, your asparagus is growing, it is growing faster than you thought and you need another group of people to come to cut it; so you have twice as many workers today as you had yesterday. We do not expect you to go on; we expect you to file every seven days, rather than literally every time you are potentially handing over, because it might be the last day of picking and you increase the numbers, and they won’t be there tomorrow. Similarly, in those trades where, if circumstances get very busy in an unplanned way, you bring in additional labour unexpectedly and then pay because they are not regulars, we are allowing people to catch up and pay within their normal rhythms.

What ICAEW believe is that there is a wider range of small businesses that need consideration. Ruth Owen and I are very keen that we understand their reservations. As I say, I was talking to ICAEW this morning, and I think it is important that we try to distinguish between organisations that are not very well organised, where we and the agents may need to help, particularly as there are some free offers that would be very easy to use and might sort out their problems, and those organisations where there is a real business dynamic that makes it hard to do what we are asking. We are determined to keep looking at that, rather than assume that we know the answers.

Q127 Mr Bacon: Yes, I hope so. I do not find it very reassuring that people running small agricultural businesses, whether they are growing asparagus or anything else, will only have to file every seven days. You are suggesting that every seven days, they will have nothing better to do than pump more information into HMRC. Frankly, it does not surprise me that the ICAEW is worried about that.

Lin Homer: We had this discussion at the Treasury Select Committee. The point that I made to Teresa Pearce, I think, was that if you are a smallish business paying cash out day after day and you are not keeping some record of that, you are going to get in a muddle yourself quite quickly. For most of what we require, if you have a system into which you are inputting what you are doing as a small business, that will be adequate for you to give us what we need.

Q128 Mr Bacon: By the way—this is slightly tangential, but in a way it is not—am I right in thinking that petrol stations selling petrol or diesel have to pay the customs or excise duty due on their sales daily? Is that correct? I was once told that.

Lin Homer: I do not know, I am afraid.

Edward Troup: Fuel duty is collected at the point at which the fuel leaves the refinery. I have seen it happen. There are tax points there.

Q129 Mr Bacon: But is it daily?

Edward Troup: It is whenever it leaves: literally as the lorries go through, all day and all night.

Q130 Mr Bacon: Pretty regularly, in other words. That was an aside. In other words, if you are a large business, you can.

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Paragraph 15 of the Report says that “At 31 May, 209 PAYE schemes covering 1.5 million individual records were using RTI” and that “By October 2013, all employers and pension providers will be required to use it.” If you were at 1.5 million individual records by the end of May, where are you now?

Lin Homer: If you look at figure 6 of the Report, we are just entering stage 3, where we are moving from about 1,300—although we have been running slightly ahead of that—to building up to having 250,000 employers on. Now that is not—

Q131 Mr Bacon: Sorry, that was not my question. My question is about individual records. It says 1.5 million individual records; my question is how many individual records you have got now, if it was 1.5 million at the end of May?

Lin Homer: I am sorry, I am not sure I can instantly give you that answer. I am sure I have it somewhere.

Q132 Mr Bacon: It is easy to talk about employers—there is a smaller number of employers, by definition—but individual records, you are talking about individual taxpayers, aren’t you?

Lin Homer: Can I give you a note? I know that within the pilots we have got, we have the full range from very small to very big, so I know that we now have a large number—

Q133 Chair: So you have got some SMEs in there?

Lin Homer: Absolutely. I apologise; I am afraid that I have got the number of employers, but I have not—

Q134 Chair: Do any of your colleagues know the answer?

Nick Lodge: I think the figure is 2 million individual records, but we will confirm or correct that.

Q135 Mr Bacon: So it is going to go from 1.5 million to 2 million?

Nick Lodge: I think it is 2 million now.

Q136 Mr Bacon: I see. Where will it be by October 2013, when all employers and pension providers will be required to use it? How many individual records will be there?

Lin Homer: It will be close to 39 million, because that is how many—

Q137 Mr Bacon: Right. And you are on track to do that by October 2013?

Lin Homer: Yes, we are.

Q138 Mr Bacon: You are confident about that, are you?

Lin Homer: Yes, I am. As I said earlier, we are actually slightly—

Q139 Chair: I want to ask you a question about your confidence. You must have seen the FSB survey.

Lin Homer: Yes, I did.

Q140 Chair: The survey suggested that a quarter did not know anything, only 16% were fully aware and only 60% had heard from you.

Lin Homer: Yes. First of all, it is partly a question of what question you ask them. We are not particularly trying to get the general public familiar—

Q141 Chair: No, these are businesses, aren’t they?

Lin Homer: Small businesses, particularly with FSB. We are not trying to get RTI as a brand, if I can put it that way. In the conversations that we have had with businesses, we have talked about changes to PAYE. Our own polling suggests that 89% of tax agents know, which is very reassuring; many small businesses will have an agent. I think nearly 50% of businesses know, which is higher than FSB thinks.

The other thing is that we had discussions with small businesses and FSB further back, at the beginning of RTI. What the small businesses said to us at the time was, “It’s very difficult if you tell us a lot about this in advance and then expect us to retain it all. Will you come back and tell us about six months before we have to do something?” We are working with the small businesses when they said it is best to do so. We have recently written to all those small businesses, and we will focus on helping them to understand and get ready in this next period.

Q142 Mr Bacon: What I want to ask you about is the stuff that will still go on at the other end. In paragraph 17, it says that the Department will still have to undertake an end-of-year reconciliation of each taxpayer’s record, as employers will not report all data monthly under RTI. “The Department needs to decide, taking account of emerging findings from the RTI pilot, on which changes notified under RTI it should update on taxpayer records in real time and whether it can carry out any of the work currently performed at the reconciliation stage earlier.” Are you clear about any of that yet?

Lin Homer: We are still looking at that.

Q143 Mr Bacon: Do you know what changes cannot be made during the year?

Lin Homer: It is not particularly “cannot”. I am sure it is value for money that the NAO is interested in. There are some changes that will become evident to us by more regular reporting that we do not need to do anything with until the end of the year. The NAO also did some work with us on the number of work management items that we can and cannot manage to do. Those that will automatically sort themselves we will not lift out and work at the first point that they become noticeable to us, so we will make judgments.

Q144 Mr Bacon: That will be your decision criteria—if it will sort itself out anyway, we will not do it. That is how you decide, is it?

Lin Homer: That is one. There is a second issue that we are looking at. Happily, it is something that we work very openly with NAO on, and there are other areas where we think there are probably system fixes where we can get some more of these in-year changes that effectively automate themselves. Again, if that avoids them being manually worked for relatively small sums of investment, we think that will be worth doing. We are just going through some further work to take some decisions about which of the work

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management items generated by RTI and NPS should be “worked immediately” or “held”. In the “worked immediately”, it is either worked automatically or worked manually, and that is work in progress.

Q145 Mr Bacon: What contingency plans are you putting in place in case RTI is delayed?

Lin Homer: We do not think that RTI will be delayed. People will keep paying us the money they owe us, so the transfer from one system to another is not a cliff edge where everything stops. On current track, we think that with the agreements we already have in place for some employers to join before and after the due date, we are confident that we can hit the deadlines for next year.

Q146 Mr Bacon: Are you saying that you don’t have a contingency plan and that you don’t need one?

Lin Homer: I tried that on the Treasury Committee, and it, like you, accused me of not explaining myself very well. What I am saying is that our contingency is, to some degree, to get ahead of ourselves and have less to do at the turn-on point, so that, for those people who are challenged at that moment, we have more resources to throw at them.

Mr Bacon: That is what the Olympics did and it worked for them.

Q147 Mr Jackson: For the sake of good order, can I ask you a question that I have asked the permanent secretary? I want your viewpoint, but I am mindful of the fact that you don’t want to veer over into political issues. The coalition agreement contains a pledge for a transferable tax allowance for marriage support that is backed by both parties in Government. There are rumours that the complexity of that in terms of tax infrastructure is such that if it is not announced in the forthcoming Budget, it just cannot happen before the general election. How difficult would it be to bring forward a change of that magnitude to enable the Government to deliver on the coalition agreement?

Lin Homer: Rather than talk particularly on that one—as you say, it is not for me to decide whether it is done—let me say that what we are trying to do, and part of the reason why I was so keen that Edward joined us, is to ensure that we are discussing with our Treasury colleagues, from the earliest moment, not just what the Treasury wants to happen but what that will entail. We are getting involved as early as we can, looking at options for the way you do things as well as what you do. We have, do we not, an open seat at the table?

Edward Troup: And I think that what we have done on child benefit is a good example of where we work with the Treasury. I was actually at the Treasury at the time to make sure that what was announced and the timing of it was deliverable operationally, as it has been.

Q148 Mr Jackson: But we don’t know that yet.

Edward Troup: No. If Ministers and the Treasury develop a new tax proposal, whether it is on transferable allowances or something else, they will work with us to ensure that the announcement is effectively deliverable.

Q149 Mr Jackson: So you modelled the scenario of, say, an announcement in March in the Budget, and you have worked back on how that would impact in terms of your practices and the architecture of delivering it?

Edward Troup: That is a question about policy that Ministers haven’t made any announcement on. They may do, or may not.

Q150 Mr Jackson: They have, actually. You are not quite correct; they have said they support the policy. The Chancellor of the Exchequer, the Prime Minister and the Exchequer Secretary have all committed to enacting the policy before the end of this Parliament.

Edward Troup: But there has been no Budget announcement, as you say. All I can say is, generically, with all Budget announcements—whether or not they actually happen—in the course of working them up, there is close working and partnership between HMRC and the Treasury to make sure that it is not just, “Yes, we are going to do this”, but “Yes, we know how we are going to do it and HMRC can deliver it.” I am not going to talk about the development of policies that have not yet got to the point of announcement.

Q151 Chair: I am going to do some more work around that. What I don’t understand in all this is that when I looked at paragraph 14 on R7—this goes back to the RTI point—20.5 million work items arise annually from changes that people currently tell you, but you can only take action on 13.5 million. If that is your performance at the moment in relation to existing systems, when you get to RTI, unless I am completely misunderstanding it, I do not understand how on earth you are going to be able to cope with all the changes that you are told all the time. RTI will inevitably add to that number, and I just don’t get it. I don’t know whether I am missing something and I need educating in the way you work.

Lin Homer: That was really the point I was trying to make about our continued work into what work items are generated, why, and whether we can do anything to automate them or get rid of them. Sometimes that will be policy changes—

Q152 Chair: But you won’t do that in time for next October, because that requires new computer programs.

Lin Homer: We are constantly making some changes. As NPS settles in and as RTI is developed, we are automating more and more of our system. I should perhaps say that the open cases, which I know you took a great interest in and which are reported on, were the consequences of a system that was generating more items than could be worked on. The first thing I would like to say is that, due to some incredibly hard work by everyone involved, we have now concluded the working of those cases.

Q153 Chair: So, before 12 December.

Lin Homer: Yes.

Chair: That’s good.

Lin Homer: The people involved really deserve acknowledgement for that, but we also learnt the

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importance, therefore, of thinking about why this work item is being generated, and what you can do. I am not going to sit here and say that we have answers to all of that, but we are determined to go through it. At the end of the day, if there are no solutions to those, we are going to have to look at the resourcing level, because after all the hard work to clear that 17.9 million, one thing that I do not think I could accept as chief executive is if we then allowed more to develop. So, we are going to look at those—I am very happy that the NAO is involved in that—and then, I and my colleagues will have some tough decisions to make if we still find that the number running that we cannot resolve automatically runs ahead of our current resourcing level.

Q154 Chair: I think I am going to have to come to understand it better, because I don't really, at the moment.

Can we move on to tax credits? From R38, figure 11 in the NAO Report, it looks like you are doing worse on fraud and error, which seems depressing, because not only did you not meet the objective set long ago on reducing that, but fraud and error are up—particularly fraud, more than error—and, of course, that means your accounts get qualified. It is a bit depressing.

Lin Homer: The accounts being qualified is really a transfer of tax credits from one of our accounts to the other. It is more material in the resource accounts, and therefore, it leads to us being qualified. I suspect that even as we improve this, we will probably remain qualified for quite a long time. Nick Lodge has recently taken over the tax credits area and has been able to have a good look at that. We have not concluded the work, but I thought it might be sensible to let him tell you his initial thoughts about what we have learnt from this and what we think we should do next.

Nick Lodge: It is clearly disappointing that the percentage of fraud and error has not reduced to 5%, as we expected it would. We measure that percentage figure by reference to an annual sample exercise, so the percentage figure—the 5% figure we were targeting—is measuring the extent of fraud and error in 2010–11, because there is a long lag. We cannot do the sample until tax credits awards are finalised for a particular year.

We have been doing some analysis. There are ever-increasing losses prevented in-year. You will notice from the NAO's Report that the losses we are preventing, the interventions that we are carrying out to identify and prevent error and fraud, are actually increasing year on year. They amounted to £1.4 billion for 2010–11, the figure for 2011–12 was £1.93 billion and the figures were much lower in the years before that. What we found is that some of the assumptions underpinning our calculation of that in-year measure—and we have calculated the in-year figures that we have been producing as being the right level of interventions to actually reduce error and fraud to the 5% target—just have not been quite borne out in practice.

Q155 Chair: Do you mean it was bigger than you thought?

Nick Lodge: We make an assumption in those figures as the NAO Report describes for an amount of deterrence; so we assume that the effect of our interventions—and there are well over 1 million a year—will be some deterrent effect. We cannot see that yet coming through in the sample. We make some assumptions for the impact of our interventions in one year carrying forward into a future year; by that I mean with an award that we put right, because we identify incorrectness, we assume that the claimants will keep that award right into a future year, in some circumstances. We made some assumptions around that. We are not seeing that to the extent that we expected.

That, together with some of our other assumptions, means that actually the impact of our interventions has not had an effect as big as we would have expected, and, indeed, would have liked, on the overall levels of error and fraud.

Q156 Chair: But you don't know why.

Nick Lodge: Well, we do know why, because we know that the deterrence that we had expected to happen—in other words, deterring other claimants because they know we are intervening in these cases: we cannot see that deterrence effect coming through. We can also see that the length of time that an award stays correct is smaller than we had expected. In other words, people are making the same mistakes in the future, more quickly than we had assumed. So the summary of all that is that we have to revisit our strategy in the light of that greater understanding, and we have to work out, now, how best to target our efforts, and redouble our efforts, to reduce the overall extent of error and fraud in the system.

Q157 Chair: Just give us an idea of the time frame around all that. When are you going to have your new strategy in place, and when can we expect to start seeing that yielding some results, and what will the results be? Or is it too early to say?

Nick Lodge: It's a little early. The full sample results that are national statistics were published in June this year for the 2010–11 year. We have been analysing those and understanding the reasons for the disparity in our losses prevented figure, and our percentage of error and fraud figure, as I just described—the deterrence and the carry-forward. Having understood that, we now have to look at whether we can retarget our interventions—whether we can improve our strike rates, whether we can improve our use of data, both internally and using third-party data, and whether we can apply greater capacity to the work. So it's a little early, but that's the work we are doing now.

Q158 Chair: What time frame? A little early to tell us the number, but presumably not too early to tell us when you are going to have thought through what you are going to do.

Nick Lodge: No, I think our strategy will be clear within the next couple of months.

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Q159 Mr Bacon: What is the total value of incorrect payments made since tax credits started?

Nick Lodge: I can tell you the total amount of overpayments since tax credits started. It amounts, to the end of March 2012, to about £14 billion, of which £4 billion was the tax credits overpayments total left at March 2012.

Q160 Chair: I don't understand that. Say that again.

Nick Lodge: Fourteen billion is the total cumulative amount of overpayments since it first started.

Mr Bacon: That is what I was asking, really.

Q161 Chair: What is the £4 billion?

Nick Lodge: Sorry, the £14 billion is the total cumulative amount of tax credit overpayments to March 2012; £4 billion is the amount of that £14 billion that remains. Of the gap—the £10 billion—we have collected £6 billion and £4 billion has been written off or remitted.

Q162 Chair: And underpayments?

Lin Homer: A smaller amount.

Nick Lodge: A very small amount. We put those right as soon as they become apparent.

Q163 Austin Mitchell: The tax credit debt—you are falling behind a bit here. Personally, I would not want you to be tougher; I would want you to extend the same generous regime you give to the big corporations to people who have been overpaid through mistakes by HMRC.

But there is a contrast between your estimate, which says that you want to get it down to £3.7 billion by March 2015—the total personal debt—but the Report says, at paragraph 4.28, based on an estimate of yours, that the Department is likely to generate £1.6 billion in new personal tax credit debt in 2012–13, so that the total could increase to £6.5 billion by 2014–15. So there is a wide gap between this estimate and your hopes of getting it down.

Lin Homer: First of all, we do have very clear rules about how rapidly we reclaim repayments, because we are aware that that can cause hardship. There are well developed rules, and I have sat and listened into some of the conversations with people—

Q164 Austin Mitchell: To achieve that total, you are going to have a big write-off, sending people rejoicing into the May 2015 election.

Lin Homer: What the paragraph does say, and they are important words, is “without any further intervention”. What we are increasingly trying to do—this is true not only of personal tax credit debt, but of debt generally—is to intervene earlier and to come to arrangements to pay.

We find in the vast majority of cases that, if we settle sensible arrangements to pay with people, they then comply with them. So I expect some further write-offs and remissions around tax credit debt—just as with all debt, some will prove to be irrecoverable—but we also expect to get some of that repaid, sometimes out of ongoing benefit payments and sometimes after benefits have stopped.

But we are getting better, we think, at spotting debt early, acting on it early and coming to sensible arrangements that do not overwhelm people and that they can then keep to. We are finding that with the “Time to Pay” arrangements as well.

Q165 Austin Mitchell: You have to have a substantial write-off before the universal credit system comes in, because it will be difficult for people to pay back these kinds of debts at the same time as seeing their benefits probably cut under the universal credit. It will be difficult to marry up the systems, won't it?

Lin Homer: We have come to an agreement with DWP that, where benefits are ongoing, some of our debt will be able to be paid back out of ongoing payments, just as it has been for tax credits. So that deal has already been done. To some extent, we are already seeing people moving out of benefit, so the changes in threshold for tax credit itself have already taken 1 million out of the eligible population—

Q166 Chair: Out of the population that goes for tax credit—so 1 million are no longer eligible for tax credit.

Lin Homer: Over the past few years because of the changes that have been made.

Q167 Chair: Okay. So how many are?

Nick Lodge: Perhaps I can help. We have about 5.5 million households in the tax credits system—

Q168 Chair: One million less than there were when? What is your 1 million?

Nick Lodge: That figure will reduce further.

Lin Homer: So to some extent we have already been dealing with people who finish up with debt but have no ongoing benefits. That was my reference to some very skilful work by our telephone operators in reaching arrangements that are manageable for the families in their new circumstances. Some of them have arrangements to pay over quite a long time. We are thoughtful about not tipping the repayment to a position where it is just not sustainable.

Q169 Mr Bacon: As a result of your own errors in the first place in paying out £2 billion every year that you should not be paying out. That is what it boils down to, isn't it?

Lin Homer: No.

Q170 Mr Bacon: Isn't it? The Report says you are paying out between £2.08 billion and £2.46 billion to claimants incorrectly. That is what you pay incorrectly each year, isn't it?

Lin Homer: Yes, but often the errors are due to the family failing to inform us of a change of circumstance.

Q171 Mr Bacon: Yes, I understand that there are issues around what the family have to do, but basically your system involves paying out £2 billion a year that you should not be paying out—and then you have to go around and correct the errors in a way that doesn't strike the fear of God into them.

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What I would like to know is this. Perhaps you do not have this answer, but lots of work goes on in the DWP—and, I imagine, also in HMRC—that is based on estimates, worked examples and extrapolation. Do you have any figure for the number of people who simply do not claim tax credits at all, because they want to have nothing to do with it, because they are fearful that they will end up in a situation where they are overpaid, even though they are entitled?

The ombudsman said something about this—that the system was fundamentally flawed in such a way that it was trying to target people who probably were not suitable for the kind of arrangements that were in place, where overpayments were inherent. Do you have an estimate for the number of people who are entitled but who do not claim?

Nick Lodge: I am sorry; I do not have that figure. We will have to—

Q172 Mr Bacon: Do you not have any idea?

Nick Lodge: Six out of 10 families do get tax credits. Take-up has traditionally been, I understand, quite high, but—

Q173 Mr Bacon: Six out of 10 of all families?

Nick Lodge: Yes. But we would need to go away and check the precise figure for the percentage that do not take up tax credits.

Q174 Mr Bacon: To your knowledge, if you do not have the figure to hand, is it a figure you are likely to be able to find?

Nick Lodge: We have certainly had that figure in the past, so I think the answer is yes, but I would need to go away and check.

Lin Homer: There is bound to be an estimate.

Q175 Mr Jackson: Can I ask you about the specific issue of child tax credits? My constituents get slightly concerned when they hear about the number of child tax credits that are going to EU citizens whose children do not reside in the UK and are likely never to reside in the UK. You will say that is a relatively small amount.

What concerns me slightly is that until recently you have not collected—or rather the Treasury has not been willing to divulge even that it attempts to estimate the number. I just wonder whether you collect data on that. Would you know how many, what countries and on what basis and, more importantly, what is the practicality of checking the veracity of those claims?

Lin Homer: We have some quite complex arrangements for checking their veracity, which do include information from the home country. That is one of the reasons why, when I write to a number of you, it sometimes takes us longer to verify and validate those tax credit claims than normal ones. I am not sure whether our system would differentiate European Union—

Nick Lodge: I have not seen those figures. We obviously carry out checks on right to reside and so on and, as Lin has just said, we check with the home country—

Q176 Mr Jackson: Well, until recently the Treasury was telling my colleague Anne Main, the Member for St Albans, that it did not really know what “habitually resident” meant for tax reasons, in terms of disbursing child tax credits, and therefore could not estimate how much money was going into that area and to whom. I just wonder whether, if you tightened up your management data collection and you knew where that money was going—okay, it might only be a few hundred million now, but it is still a cause of concern to a lot of people.

Lin Homer: We do not have it to hand.

Q177 Mr Jackson: Will you write to me with that information?

Lin Homer: We will be very happy to let you know whether we do think that can be extracted from the system. I think to a degree our system is required to be blind to European status, so it is just a question—

Q178 Mr Jackson: Not necessarily. If you had been listening to the debate on my European Union Free Movement Directive 2004 (Disapplication) Bill last week, you would know that is not necessarily the case.

Lin Homer: Understood.

Mr Jackson: I’ll send you a copy.

Q179 Chair: I want to ask you three short questions. This one is on PAYE—the reconciliation on PAYE. Your latest figure is £53.7 million for the tax that has been lost through various things—money coming in too late and getting money out of people late. You are also raising the level at which you pursue people. What is the final total? If you have finished all these reconciliations, what is the final total of moneys lost to the Exchequer because of the mess in which this reconciliation occurred over time?

Lin Homer: I believe we have come in within that figure. There are two aspects: one is the resource that it has cost us, and the other is the sums that we have agreed to forgo. The figures in relation to our forgoing are now dropping back down, because we have dropped back down to the £50, rather than the £300. One of the challenges for us—I have the figures somewhere; I apologise, because I temporarily cannot find them—is that the new system counts the £50. The old system just ignored the amount under £50. It did not count it. In the new system, although we still forgo it, we account for it, so you are going to see slightly bigger sums that are written off going forward, because it is now a more accurate figure. We absolutely do have them—

Chair: Maybe somebody behind you can find them while I ask you the other two questions.

Lin Homer: Yes, or if I get someone to answer the other ones, I am sure I—

Q180 Chair: Somebody can pass you a little note.

I notice in the Report that you say that your performance on answering the telephone has improved, but it is pretty shocking that one in four calls does not get answered.

Lin Homer: I did not think it was good enough—you are right—and that is really why I wanted to put extra resources into the contact centres. I have to say that

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at the last check, we are over 90% now. We are traditionally a bit higher at this time of year, and what happens is that we do not sustain that, so the extra thousand people—

Q181 Chair: It should be 100% full stop, or 98% or 99.9%. If you ring about tax, you should be able to get an answer.

Lin Homer: It was 96% last week. You still lose a few, because people drop out themselves—they suddenly realise that they do not have their NI number or whatever, so you always lose some—but we believe that if we can get it to 90% and keep it to 90%, several things happen. One is that the call waiting time for everybody drops enormously, because people are flowing through the system accurately. The second is obviously that people feel a lot less frustrated by the time they get to speak to someone, and hopefully the conversation is easier, sharper and more productive.

What we believe will also happen is that people will have more confidence in the system, and will call when they need to and not worry. At the moment, we find that loads of people worry over a weekend and then try and call on the Monday. Mondays are the worst day of the week to call the call centres—don't call on the Monday, I would say. If people feel more relaxed generally, we think it will spread out. We are open eight to eight five days a week, and eight to four on a Saturday. It is not, "Nobody call on a Monday", but if fewer people called on a Monday, the wait would be smaller.

Amyas Morse: I do not wish to cut across that excellent explanation, but we are publishing a Report on customer service in HMRC very shortly. There are some issues about just what we count as answered calls, as I am sure you know, Ms Homer. The Report sees the situation as a little bit less satisfactory than you have outlined, but let us see how that goes in the Report.

Lin Homer: In the year as a whole, it will still be around 74%.

Q182 Chair: My very final question is that I wrote to you on 31 October, reminding you that the Committee expects an answer to the letter we sent to Mr Inglese on 17 October. Can I just know from you when we can expect an answer from Mr Inglese?

Lin Homer: You also wrote to me about another matter very recently, on which I owe you a reply. I have signed that one off today, and I will—

Q183 Chair: No, this is about expecting an answer from Mr Inglese.

Lin Homer: I know. I am content that probably both he and I will write to you again, Chair, and I would

be very happy, once you have got the letters, if you wanted to talk further with me.

Chair: Say that again.

Lin Homer: I will write to you as well, and I would be very content to talk with you further, if you and the Committee wanted me to.

Q184 Mr Bacon: Do you mean as well as Mr Inglese?

Lin Homer: Yes. It remains an issue where the difference between us is something that I would like to resolve and to get clear, so in addition to writing I would be happy to have a meeting with some or all of you, if you felt that that would be useful.

Q185 Mr Bacon: Can you name any private sector organisations that pay out £2 billion a year which they should not do, and which answer only three quarters of their telephone calls?

Lin Homer: I would aspire to not be in that position, but there are not any private sector companies that act as the welfare net that we do, through tax credits. One of the points Mr Mitchell made is that we have to pay, even when we think that there may be an error, to ensure that the family is not put at risk, and we then pursue the detail afterwards.

Q186 Chair: And the scary thing is tax credit, child benefit and RTI.

Lin Homer: It is a busy department at the moment; I will give you that.

Q187 Mr Bacon: Is there any extra complexity you would like the Government to add on? Tell me about the complexity gnome, because the Treasury Committee asked you about that, didn't it?

Lin Homer: We had an interesting discussion about whether tax could be simplified as well, and I was saying that I was not holding my breath waiting for that. I think the new team is in good shape, and that we believe we are improving. I hope you will find that we will be straightforward with you about the concerns we have, as we were on tax credits today. I have no doubt we will continue to be the topic of conversation for you on regular occasions. I am looking forward to seeing you on 6 December.

Q188 Chair: You will, and I look forward to seeing you again before us. Thank you very much indeed.

Lin Homer: I will give you a note on those figures I have got, which I could not find. I apologise.

Mr Bacon: Thank you.

Monday 12 November 2012

Members present:

Margaret Hodge (Chair)

Mr Richard Bacon
 Stephen Barclay
 Jackie Doyle-Price
 Meg Hillier
 Mr Stewart Jackson

Fiona Mactaggart
 Austin Mitchell
 Nick Smith
 Ian Swales

Amyas Morse, Comptroller and Auditor General, National Audit Office, **Gabrielle Cohen**, Assistant Auditor General, NAO, **Paul Keane**, Director, NAO, and **Marius Gallaher**, Alternate Treasury Officer of Accounts, were in attendance.

Examination of Witnesses

Witnesses: **Troy Alstead**, Starbucks Global Chief Financial Officer, **Andrew Cecil**, Director, Public Policy, Amazon, and **Matt Brittin**, Google Vice President for Sales and Operations, Northern and Central Europe, gave evidence.

Q189 Chair: You seem a very long way away, so apologies for that. That is the way this room is set up. Can I thank you all for agreeing to come and give evidence to this Committee this afternoon? The purpose of our session is to get some understanding of the way in which you manage your financial arrangements and to try to understand why you don't pay the corporation tax that it appears, on the facts, is due. That is the issue that we are focusing on this afternoon.

I thought to start with, if this is all right with you, we would go one by one—your circumstances are all very different—to try to get some understanding of the individual circumstances, and then move to some general questions, which I think impact on all three global companies. Our particular interest, of course, is that now that so much of UK business is carried out by global entities, corporation tax, and the way in which tax is collected, is hugely important. All three of you are American-based companies, which is also of particular interest. Can I start with Starbucks, Mr Alstead? My understanding is that you filed, in Companies House, losses for most of the years that you have been running coffee houses in the UK. Is that right?

Troy Alstead: Yes, that is correct.

Q190 Chair: Yet if I take you through some of the statements that we have seen, in 2007, which was the 10th consecutive year that you filed losses, your chief financial officer at that time—he must have been a predecessor of yours—Peter Bocian, said that the unit enjoyed operating profit margins of 15%. How do you reconcile those two?

Troy Alstead: Respectfully, we have never seen any record that there are any statements that the operating business in the UK made 15%. We did have one year of profitability. That was in 2006. It was a very small profit, unfortunately, due to reasons that I am happy to discuss with the Committee, and I appreciate the opportunity to have this discussion today. But in all of the context of the historical public transcripts we have found—the analysts' reports that have been published; all of our press releases—they have all spoken to our challenges in the UK and our targets

for the UK going forward, and they have very consistently spoken about our difficulty around profitability.

Q191 Chair: This report of a 15% profit rate was in one of the many briefings that you gave to your shareholders. That is my understanding. So what was the true rate of your profits in 2007?

Troy Alstead: The UK Starbucks business made a loss in 2007. It made a profit in 2006 for the first time, which perhaps was a reference point in 2007, made in the previous year. But that was the first profit the company made and it was a very, very small £6 million profitability in that year.

Q192 Chair: As I understand it, there were 46 separate conference calls. Let me take you to 2008. You filed losses in the UK companies accounts of £26 million, yet Schultz told analysts that the UK business was so successful that he planned to take the lessons learned here and apply them to the USA. I understand that year, or maybe a year later, he promoted Cliff Burrows, who was head of the UK and Europe business to head up the US business. That sounds a bit odd: on the one hand you were claiming losses in the accounts you were filing in Companies House, but on the other you were promoting profits and promoting the individual responsible for the UK business.

Troy Alstead: We have always been, number one, optimistic about our ability to turn the business into profitability here. We have had huge—

Q193 Chair: How do you explain the difference? I am sorry to interrupt you. As I understand it there are transcripts of the conference calls—right? So I don't think anybody around the table is making it up. I am certainly not making it up. If you have these conference calls which tell one story and accounts that tell another, and you then promote the guy responsible for the UK business to run your US business, it just doesn't match. It doesn't ring true.

Troy Alstead: We are required to speak to and file our accounts in the UK—

Q194 Chair: Are you lying to your shareholders?

Troy Alstead: Absolutely not. Absolutely not.

Q195 Chair: Well, how can you reconcile the two businesses?

Troy Alstead: We are required to report our accounts in the UK under one standard. We are also required under US accounting to speak to our profitability in a different way, to eliminate all inter-company transactions that are involved. So those are requirements that we have to meet both in the UK and the US. There is a difference between those two.

Q196 Chair: But you were talking to UK investors here?

Troy Alstead: In our transcripts and our conference calls?

Q197 Chair: That is my understanding. I can take you to 2011: losses of £33 million, and John Culver, president of the international division, told investors, “we are very pleased with the performance in the UK.” Yet you filed £33 million losses.

Troy Alstead: We have been encouraged by our ability to drive top-line sales and growth in this marketplace.

Q198 Chair: But you are not making money.

Troy Alstead: No.

Chair: Or you tell us you are not making money.

Troy Alstead: No. I assure you we are not making money and the investors we are speaking to are all of the investors in the company. We have never targeted just to the UK, although we understand that audience. In all earnings releases and conference calls, our primary message has to be under the SEC rules for the US, which are addressing primarily US-based accounting rules and reporting rules.

Q199 Chair: But you are talking about the UK business?

Troy Alstead: Yes. And we are required in the US to speak about it under US rules.

Q200 Chair: I understand that when you talk in the US you take out the royalties, which no doubt we will come to. But it still seems very odd to file losses and then tell your US investors—or your global investors—that you are pleased with the performance in the UK and to promote Cliff Burrows. Why did you promote Cliff Burrows?

Troy Alstead: Cliff Burrows helped us turn the UK from perpetual losses into the one year of profitability. We saw consistent improvement under his leadership.

Q201 Chair: Only the one year you are admitting to.

Troy Alstead: That is correct. Those are results that are—

Q202 Chair: The other thing that is odd to me is that if you have made losses in the UK over 15 years, which is what you are filing, why on earth are you doing business here?

Troy Alstead: We know that we must be in the UK to be a successful global company.

Chair: But you are losing money here.

Troy Alstead: It is a critical market.

Q203 Chair: Why don't you go over to the US and focus on the US, where you say you are making money—if it's true?

Troy Alstead: Because we have had tremendous optimism and encouragement over time about our ability—

Q204 Chair: You have given the UK business 15 years, Mr Alstead. You are still making losses, and yet you are carrying on—if it's true.

Troy Alstead: Yes, I assure you that it's true. It is very unfortunate. We are not at all pleased about our financial performance here. Everything we are saying and everything we have said historically is fundamentally true.

Q205 Chair: It just doesn't ring true. The two are inconsistent. You have run the business for 15 years and you are losing, and you are carrying on investing here. It just doesn't ring true.

Troy Alstead: We are committed to this marketplace and to our customers. We know that to be a successful—

Chair: Yes, but you are losing money.

Troy Alstead: To be a successful global company we have every intention to make this market successful and profitable.

Q206 Chair: And you have tried for 15 years and failed, and you have promoted the guy who failed over 15 years and succeeded in one year only. That just doesn't ring true, Mr Alstead. That is what frustrates taxpayers in the UK. You've got to give us a better explanation.

Troy Alstead: Occupancy costs on our P and L in the UK are two and a half times higher than in our US business, for example.

Q207 Chair: Your what costs?

Troy Alstead: Our property costs—occupancy costs. They are about 24% or 25% of turnover in this market. Much of that has to do with strategic mistakes we have made in the past around the concentration of very high costs, with high street locations concentrated within the city of London rather than being perhaps more diversified around the country. That model just does not work in a coffee shop environment for us, so we have been systematically having, unfortunately, to close stores in the last handful of years, to begin to remove that burden from our P and L. In fact, we recently announced 22 more stores where we have agreed with landlords to pay out of the leases.

Chair: I understand the issue about property costs, but I just do not believe that any corporate entity would sustain so-called losses for 15 years and carry on with the business, or expand it.

Q208 Stephen Barclay: On that point, Mr Alstead, if that is the case, in your submission to the Committee at paragraph 1 you say that you plan to open 300 new stores up and down the country.

Troy Alstead: Yes.

Q209 Stephen Barclay: What return on capital are you saying to investors that they should expect, given that you have been running at a loss for so many years?

Troy Alstead: As we open new stores, each new store, if it is company-operated, has to go through a full return-on-capital analysis to meet those on-paper hurdle rates. Our challenge in the UK is that historically we have not met those achievements, unfortunately, but many of our stores in the UK going forward will also be licensed stores, similar to some strategies we have in Europe, which tends to give us a better opportunity to have a more successful financial model.

Q210 Stephen Barclay: So when do those investors expect to see a return, on those additional stores?

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Troy Alstead: Our investors are very clear on our challenges in this marketplace, and I think that they are sceptical of the history we have had in terms of our ability to immediately turn it around. But it is very transparent. There is a very good understanding of what our ability is to improve the marketplace going forward, but they are very clear on what the losses are. That is reflected in all the reporting they have published.

Q211 Chair: Mr Alstead, we are sceptical of your story. I think the allegation is that the way in which you set charges against the UK business means that you manipulate the profits out of the UK into tax havens.

Let me take you through the charges that have been put in public. The first is that you charge for intellectual property. I gather it was originally 6%, and I understand that somehow there has been a negotiation with HMRC and it is now 4.7%. I have to tell you that I am a coffee addict, so I drink far more coffee than is good for my health. I cannot tell the difference between a Starbucks coffee and one from Nero, Costa or anywhere else, so perhaps you can enlighten me. I can, however, tell the difference between a McDonalds and anything else, and I can tell the difference between KFC's drumstick recipe and other chicken takeaways. I cannot understand this great intellectual property that we are paying for, whether it is 6% or 4.7%. I just do not get it. Perhaps you can explain how on earth you reach that figure.

Troy Alstead: I will try to. Licensors, as you have mentioned with all the other brands, typically assess for their licensees these fees to represent goods and services. These are very tangible costs associated with product innovation, store design and trademark protection. All of those activities—

Q212 Chair: Let us be generous to you. Let us stop the 6%, although I am really fascinated as to how you went from 6% to 4.7%. How much of the 4.7% is because of the fantastic skill, which is actually in America and not wherever this stuff ends up—where does your stuff end up? I do not even know. Do we know?

Stephen Barclay: Amsterdam.

Chair: After Amsterdam, does it go to Bermuda?

Troy Alstead: No. We have absolutely no tax—

Q213 Chair: Where does it go from Amsterdam?

Troy Alstead: Half of it stays in Amsterdam¹ and half goes back to the States. We have no tax havens in Bermuda, Cayman or anywhere else around the world. We never have and never intend to.

Q214 Chair: How much tax do you pay in Amsterdam?

Troy Alstead: All the royalties that leave the UK—the 6%—are assessed at a net rate over the last five years of about a 16% royalty rate. That is a mixed rate because some of that is taxed in the US and some is taxed in the Netherlands, but it is fully based at 16% over the last five years.

Q215 Chair: Let us just go through it. With the 6%, what are we paying for? For the UK taxpayer, who forgoes the corporation tax, how much are you charging for the design of the building?

Troy Alstead: We launched, for example, a new product—

Q216 Chair: How much are you designing with your 6%? How much of the 6% goes on the design of the building?

Troy Alstead: It is not articulated beneath that which components sit in it. It is an all—

Q217 Chair: There must be some figures underpinning.

Troy Alstead: No, there are not. It is an all-in fee that we have triangulated on over the years to represent—

Q218 Chair: There are no figures underpinning.

Troy Alstead: There are no detailed figures that represent which pieces of product innovation versus store design—

Q219 Chair: So how on earth do you then get that 6% or 4.7% is the fair and proper charge?

Troy Alstead: Two or perhaps three ways. One is understanding what global brands charge for those goods and services to licensees around the world. In the UK, that ranges from close to 5% up to a maximum of 8% or so.

Q220 Chair: No, it does not. McDonald's is about 4%. Burger King is about 4%. KFC do not charge anything.

Troy Alstead: The royalty rate, as we have seen around the world, ranges from that 5% or so—

Q221 Chair: This is really interesting, so you go for what is in the market—what you think you can get away with—and charge it.

Troy Alstead: We have approximately 20—

Q222 Chair: Is that right? Have I understood that right? You look at what the going rate is in a particular jurisdiction and charge it.

Troy Alstead: No, that is not quite right. If I may explain—

Q223 Chair: But you have no figures underpinning it.

Troy Alstead: We have 20 licensees around the world who are independent companies. These licensees are big, sophisticated companies who willingly pay us the 6% royalty, because they clearly recognise the value of the goods and services, the store design, the trademark protection and the value of the global brand that comes into that band. I would also point out that, whereas most licensors charge their licensees multiple fees—a royalty and often a marketing contribution and other funds—in Starbucks we have one. We have just that 6% royalty fee.

Q224 Chair: I want to understand. I am going to turn to Stewart, but I will give you one last chance. Apart from it being the going rate in a country, what are the figures that underpin it? How much for getting the coffee mix right? How much for getting the advertising right? How much for getting the layout of the shops right?

¹ Note from witness: To clarify, the reference to “Amsterdam,” is to our Amsterdam structure. Our Amsterdam structure involves a Dutch tax ruling and includes Starbucks wholly-owned European entities. The European royalty payments flow through the structure including the payments made to Starbucks U.S. for the original intellectual property and current intellectual property development costs. The Dutch tax ruling is an agreement with the Dutch tax authorities that provides advance certainty on transfer pricing aspects embedded in the formal advance pricing agreement. The transfer pricing of the transactions within the structure are arm's length and in accordance with transfer pricing guidelines set forth by the Organisation for Economic Cooperation and Development (OECD)

Troy Alstead: It is a collective fee that represents all those services.

Q225 Chair: But how much on each? There must be some logic to it, or it is just what you hope you can get away with.

Troy Alstead: It is negotiated with third parties around the world that validate that the value is there in that 6%. That is the best single way we have of recognising—

Q226 Chair: Who are the third parties? The tax people?

Troy Alstead: We have third-party licensees—large, independent companies all around the world—that also pay the 6% royalty when they license the Starbucks brand in their particular marketplace. That is our best way of understanding, in addition to analysis and benchmarking with other licensors, that that 6% goods and services charge—the royalty rate—is appropriate and justifiable, and it is scrutinised by tax authorities all over the world to validate both sides of that equation.

Q227 Chair: I am not getting a clear answer. I will have one more go at it. Most of your 6% is charged on your wholly owned subsidiaries, but in Germany you have a joint venture with Karstadt, where I assume that you have charged something like that to the chief executive, who may already have pulled the deal because he is losing money on it. So where there is a genuine arm's-length relationship, money is being lost. He said, "It is not possible that all the burdens are just on our side and then if money is made, it all goes to someone else."

Troy Alstead: We are actually in a wholly-owned business in Germany now. We bought out Karstadt as of three or four years ago.

Q228 Chair: Right; a wholly owned business, because he couldn't stand the 6%. He couldn't take it—so where you have got a genuine arm's-length principle it does not work.

Troy Alstead: And we have 20 arm's-length licensees today, the vast majority of whom make money at that 6% and are rather willing to pay us that price.

Q229 Chair: I think it is about tax avoidance.

Troy Alstead: And we would be very pleased to provide that detail to the Committee if it would be helpful.

Q230 Mr Jackson: I think Henry Ford said the business of America is business; it is a good thing he was not listening to Starbucks, because I do not find your business model very compelling or convincing, if I am honest. I think the heart of this debate is about what you do and where you do it. I would like to ask a very straightforward question. Given that the Starbucks brand is very well established, can I ask you what unique proprietorial aspect of the generic coffee-making process you own in order for you to make these payments?

What you do is exactly what Costa Coffee do, and all the other coffee companies. It seems to me that this is a system specifically designed to avoid tax and I do not think there is any evidential basis—if I could put it to you—that you have any proprietorial ownership, in terms other than brand, which is completely different from intellectual property rights. It is just about avoiding tax, which is why, for instance—and maybe

you will address this issue—you buy your coffee through Switzerland.

Troy Alstead: Respectfully, I can assure you there is no tax avoidance here. We have a global tax rate of 33% around the world. Our tax rate outside of the US is 21%, as it will be filed with the SEC next week. That is higher than most multinationals' global tax rate. We are an extremely high taxpayer. We clearly are not aggressively looking to avoid tax, or looking to avoid tax on any structure anywhere. We have had profitability challenges—very sincere ones, unfortunately, that we are not pleased with—but it is nothing, I assure you, to do with any tax avoidance².

Q231 Mr Jackson: But can you name me one company—one multinational company, one US-based company—that has a 31% market share by turnover and has been making losses for 15 years?

Troy Alstead: No, I could not be an expert on other companies. I would not pretend to be that. I am happy to discuss how our business has been challenged, and what we are trying to do about it here, very sincerely, and why we have had years of loss-making in this marketplace.

Q232 Mr Jackson: My last question, then. Are you saying that essentially the value created is created in Switzerland or the Netherlands, and not the UK; so when I buy a cup of coffee in the UK the value for the purposes of tax and tax collection is created in Switzerland or the Netherlands, and not when I buy the coffee? That is what, essentially, you are saying.

Troy Alstead: What we are saying is we should have a business that makes a profit in the UK, and that is fully our goal, and fully our intent, and exactly where we have been aiming for many years, here. We have not been successful doing that; but, yes, there is value created by the local business everywhere around the world. That value should result in profitability. That is fundamentally, absolutely our goal to do. There is no intent to do anything different from that. I will acknowledge to you we have not been successful at that in the UK.

There also is a very tangible, specific value that is created in Amsterdam, in the Switzerland office, which I am happy to talk about at any point in time,

² Note from witness: To clarify, as a responsible corporation, we strive to follow the letter of the law and have done so in the case of our tax obligations. All taxes owed to the UK have been timely and fully paid. We also acknowledge that as a profit-making company, we do avail ourselves of the benefits of the tax laws in each country in which we do business, including any favourable tax treatment of our business operations provided by the UK. We have a European regional tax structure that results in an effective tax rate of 16% on our royalties. There is much discussion of tax havens and tax avoidance. Unlike many companies and individuals, Starbucks does not use island offshore tax havens which welcome shell, not operating, companies usually run by one person with multiple entities under his or her control, and that traditionally have a tax rate of zero. Such tax havens are drastically different from Starbucks situation. Starbucks has centrally located its Europe Middle East regional headquarters and roasting plant in the Netherlands in which it employs approximately 220 persons, benefits from a multi-language work force and operates a 9,206 sq. metre coffee roasting facility, headquarters and distribution centre. Approximately 6803885 kg of coffee are distributed to multiple countries from the Netherlands. Starbucks does engage in legal tax planning to reduce its tax liability, but only where permitted by law, and never through the use of island offshore tax havens.

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and in the US, where some of the product innovation still happens, to a great degree, around recipe development. We have launched a new product here in the UK just this summer called “Refresha” that was in test and development for two years. The UK business had no cost basis in that whatsoever. A new machine platform, called the Verismo—equipment which we have just launched here in the UK—

Q233 Mr Jackson: It’s a cup of coffee. It’s not an internal combustion engine. I take the point about branding and advertising, but the generic coffee-making process is not that difficult.

Troy Alstead: We spend half a billion dollars a year in the categories of research and development, product development, category management, store design—that is at the global, not the country, level.

Q234 Fiona Mactaggart: But in what country are those sums spent?

Troy Alstead: Largely in the US, some in Amsterdam, some in a few other markets around the world; but largely in the US, which is where the vast majority of our headquarters are. That includes things like engineering services in the store, store design and layout, and lean principles around store operations. That is what we, in our big bucket, call the Starbucks system—the way to operate our stores—which over time in most places around the world has resulted in a very healthy, profitable business model. In a handful of markets we have not been successful with that, unfortunately.

Chair: I have a whole list of people, just to tell you all that you are on there: Austin, Steve, Meg, Fiona and Ian.

Q235 Austin Mitchell: Mr Alstead, my heart is beginning to bleed for you. I am going to have to rush down Victoria street and have a double caramel macchiato, because you are in such a bad way. In 14 years of trading in this country, you have paid £1.6 million in corporation tax. You are either running the business very badly, or there is some fiddle going on. I will just compare you with Costa which, in the year ending 3 March 2011, made a profit before tax of £49.5 million, and paid £15.5 million in corporation tax on that. You get away scot-free.

Troy Alstead: In the UK, one of our challenges is—

Q236 Austin Mitchell: That is quite an achievement, isn’t it?

Troy Alstead: I would argue it is not an achievement; it is a failing. The single most competitive coffee and espresso market anywhere in the world where we operate is here in the UK. There is some outstanding competition. Consumers have much choice. They likely have more choice, for consumption of coffee per capita, than probably anywhere else in the world, in terms of the contemporary—

Q237 Austin Mitchell: I have been putting on weight drinking enormous quantities of caramel macchiato and you’ve been losing money on it. It really is incompetent. Either that, or it is the money you are taking out through the 6% royalty. Now, you will not tell us where that 6% royalty goes. Surely it needs to be quantified if we are to have faith that it is not a way of fiddling money out of this country.

Troy Alstead: I am happy to tell you exactly where it goes. The full 6% goes to our regional headquarters

in Amsterdam. That is where we have a roasting facility, and all the regional headquarters for our Europe, middle east and Africa businesses are headquartered in Amsterdam. That has been there for many years now. Ultimately, about half of that funding that goes to Amsterdam ends up going directly back to the US, compensating the US for the historical development of the brand, the product innovation and our store design systems—many of the activities that have happened there historically. That is where it is. The remainder—the other half, approximately—sits in Amsterdam supported by the structure of that leadership team, and that operation³.

Q238 Austin Mitchell: You say in your notes here that some of it goes to accountancy services. We have more accountants in this country than in the entire European Union combined. There must be accountants thrusting for work in this country, but we will let that pass. You must also be charging excessively on the roasting of the coffee in Amsterdam by perspiring Dutch people and then the purchase of the coffee in Switzerland. You are overcharging us on those two items.

Troy Alstead: We sell coffee around the world at exactly the same price to all our fully independent licensees, who are big companies, as well as to our company-owned businesses. We don’t differentiate prices by country. It is exactly the same price everywhere. It reflects the fact that the coffee we buy is actually the top 1% or 2% of the most expensive coffee in the world. We have 100% fair trade espresso in the UK, and there is a premium that comes with that. We have very costly—it is very important to us, but very costly—operations with our agronomy offices around the world around sustainability and transparency. All those things yield the cost of the coffee.

Q239 Austin Mitchell: But can you tell us the difference in price between what you are paying and what competitors are paying? That is the crucial point. We do not know whether you are overcharging us or not, because the figures are not published.

Troy Alstead: I do not know what competitors pay for their coffee—I do not have that information. Our coffee costs are confidential, sensitive information. I am happy to share that with the Committee, and if I can do so in confidence subsequent to this meeting, I will absolutely do that.

Q240 Austin Mitchell: When the profits go to Holland—Amsterdam or wherever—is this all? You say the royalties are remitted back to the US. What about the profits on the European and British business? Are they remitted back to the US, in which case you will have to pay tax on them, or do they go to the Caribbean—Bermuda or somewhere?

Troy Alstead: We have no tax structure whatsoever in the Caribbean, Bermuda, Cayman or anywhere else in the world. I can assure you of that. I would like to say that very clearly⁴.

Q241 Austin Mitchell: So it is not stashed away in some tax haven.

Troy Alstead: Absolutely not. The profitability remains in Amsterdam. The profitability that we earn

³ Note by witness: see footnote 1

⁴ Note by witness: see footnote 2

in our global coffee buying operation remains in Switzerland. Some of the funding goes back to the US. We absolutely have none of these offshore island tax havens. We never have; that is just not how we do business⁵.

Q242 Chair: Can I ask a question about that? You are paying on royalties in the Netherlands, aren't you? Is there a special low-tax regime in the Netherlands on royalties?

Troy Alstead: Yes, there is. We have a tax ruling that we have had since—

Q243 Chair: So it is less.

Troy Alstead: Oh yes, it is a very low tax rate.

Q244 Chair: So there is a tax advantage to you from paying the royalties in the Netherlands.

Troy Alstead: It is a favourable tax rate that we have in the Netherlands on all income that comes in from all over the—

Q245 Chair: That is why you put it into the Netherlands.

Troy Alstead: It is not why, but it is an attractive reason to be there, there's no question.

Chair: No, it is why.

Q246 Stephen Barclay: What is the tax rate you pay in the Netherlands?

Troy Alstead: I am very happy to provide that to the Committee, but I am bound by confidentiality to the Dutch Government on that. My request would be: could I follow up afterwards and provide it just to the Committee? I am very happy to do that—just confidential⁶.

Q247 Chair: Confidential to whom?

Troy Alstead: The tax authority, under our Dutch ruling, has asked us not to share that publicly. I will absolutely share it with the—

Q248 Stephen Barclay: You have just answered my next question, which was whether you have a Dutch tax ruling—you do.

Troy Alstead: Yes, we do.

Q249 Stephen Barclay: You have a special arrangement to allow you to pay less tax in the Netherlands.

Troy Alstead: Yes, it is a low-tax ruling that we have in place.

Q250 Stephen Barclay: And it is for that reason that you transfer the profits from the UK, which are booked as losses in the UK, into the Netherlands. Some of that then goes back to the States, but the rest of it pays a lower rate in the Netherlands under a Dutch tax ruling. That is correct, is it?

Troy Alstead: Respectfully, that is not at all the—

Q251 Stephen Barclay: In what way is it incorrect?

Troy Alstead: Respectfully, that is not at all the right characterisation. Again, we have a higher tax rate than just about any other multinational around the world.

Q252 Stephen Barclay: Would you enter into a Dutch tax ruling that meant paying more than the publicised rate in the Netherlands?

Troy Alstead: I—

Q253 Stephen Barclay: Self-evidently not. The whole purpose of a ruling with them is to pay less tax, surely.

Troy Alstead: The purpose of operating our business out of the Netherlands was that we had a roasting plant facility there, and, yes, they do offer very competitive tax rulings—it is not unique just to Starbucks.

Q254 Stephen Barclay: How many people work in the Netherlands operation?

Troy Alstead: Approximately 250 people⁷.

Q255 Stephen Barclay: Including the roasting. How many in corporate headquarters?

Troy Alstead: Approximately 75 to 100⁸.

Q256 Stephen Barclay: And how many people work in the Swiss operation?

Troy Alstead: I believe that our global coffee buying operation perhaps has 30 people⁹.

Q257 Stephen Barclay: Thirty people. And what mark-up do you apply to the coffee you buy in the Swiss operation before it is transferred?

Troy Alstead: The margin that Starbucks makes on coffee that is sold to the UK and everywhere else is approximately 20%—that is the gross margin on that product sale, which is a very consistent wholesale margin on any product anywhere.

Q258 Stephen Barclay: So what do the 30 people in Switzerland do to account for that 20% mark-up?

Troy Alstead: They run all our global buying operations, they run our sustainability programmes, and they have all the agronomy offices that we operate around the world in the growing regions, where we work with farmers around sustainability, transparency and social programmes—that is all run out of our global buying operation. They ensure that the quality of the coffee is appropriate. All the coffee that we buy globally, including what goes to the US, runs through that central buying operation. Switzerland is a world-recognised coffee-buying place—75% of the world's coffee is traded through Switzerland, and Starbucks is only a small fraction of that. That is what led us to be there.

Q259 Stephen Barclay: And how do you come to the figure of 20% from that?

Troy Alstead: That is benchmarked, based on transfer-pricing regulations in tax authorities all around the world. It represents a cost that ensures there is an appropriate level of profitability on activities in the markets where they happen. For example, in all our history in the Switzerland market, we have generated an operating margin that reflects the profit generated on the mark-up on the sales of our coffee. There has been an approximate net profit in the single-digit range—7% or 8%—throughout all our history there.

Q260 Stephen Barclay: Just to confirm, the coffee does not physically go to Switzerland, does it?

⁷ Note by witness: There are 220 people working in the Netherlands operation.

⁸ Note by witness: There are 220 people total working at the Netherlands corporate headquarters, including 89 in the roasting plant and 40 in the supply chain and distribution operations.

⁹ Note by witness: There are 25 people in the buying operation and 16 people in the agronomy offices, which the buying operation oversee.

⁵ Note by witness: see footnote 1

⁶ Note by witness: To clarify, Mr Alstead is referring to the mutual understanding of confidentiality relating to information shared with and received from the Dutch tax authorities in our confidential but arm's length negotiations with them. We do not have a formal written confidentiality agreement with the Dutch tax authorities.

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Troy Alstead: The coffee is bought in Switzerland and then shipped to our roasting facilities around the world.

Q261 Stephen Barclay: It is bought there. Does it physically go to Switzerland?

Troy Alstead: No.

Q262 Stephen Barclay: So it is bought in Switzerland, and it never physically goes to Switzerland, but you add a 20% mark-up in Switzerland.

Troy Alstead: To support the activities of that operation, which yields a single-digit profitability in Switzerland.

Q263 Stephen Barclay: And that is a wholly owned subsidiary of the group. I will come back to that point later, but let me turn to the earlier point about royalties—the 6% that you said, in paragraph 16 of your submission, had, under discussion with HMRC, reduced from 6% to 4.7%. As a result of that reduction, how much more tax did you pay?

Troy Alstead: We had one taxable year of profitability in the UK in our history, so one year where we would have paid corporate income tax. Now, we paid \$25 million to \$30 million in other taxes that Starbucks pays in this market every year, but the corporation—

Q264 Stephen Barclay: We are not here to discuss the other taxes; the other taxes are a separate issue. With respect, my question was: as a result of that reduction, how much additional tax did you pay?

Troy Alstead: We paid an additional tax of approximately £8 million as a result of that.

Q265 Stephen Barclay: And what has your turnover been between 2003 and 2008?

Troy Alstead: Our turnover in 2008 by itself, for example, was £374 million. In 2007, it was £328 million; in 2006, it was £287 million.

Q266 Stephen Barclay: Are you aware of any case with any major firm in which HMRC has litigated over corporation tax?

Troy Alstead: No, I am not.

Q267 Stephen Barclay: As far as I am aware, it has not. It just looks like something of a cosmetic fight if it is being reduced from 6% to 4.7%. Financially, the impact is £8 million.

Troy Alstead: It is reflective of the challenges that HMRC put to us over time, given our perpetual loss making. We had believed that our royalty rate was fully supported and justified, as I have said. It challenged us, and that resulted in that settlement down at 4.7%

Q268 Stephen Barclay: Can you explain this, please? In the accounts for the Starbucks Coffee Company UK Ltd, you transferred £50 million into equity in a business that has been losing money year in, year out. Can you explain why you moved £50 million from cash into equity, please?

Troy Alstead: Yes, that was because the business has been losing money. As a result of our challenges with profitability in the UK, the UK business has not been able to make its payments—it has not been able to meet those cash needs alone—so it has needed the infusing of cash. Effectively, there is an inter-company loan between the US Starbucks business and the UK Starbucks business over a period of time. Essentially, that was simply the funding of that business. That was

what was represented by that loan. Tax authorities on both sides of that transaction—on both sides of the ocean—require that that be an arm's length transaction, so the interest rate was set at arm's length rates during that period of time.

Q269 Chair: Higher—higher than anybody else.

Troy Alstead: Right now that rate would be about 4.9%—

Q270 Chair: Yes, that is higher than anybody else that we have come across—to your own wholly owned subsidiaries. It is a bit odd. These are wholly owned subsidiaries and you charge a higher interest rate. The only explanation can be to get money out of the UK to avoid tax.

Troy Alstead: No, because that loan is to the US business. Actually, the US has a substantially higher corporate tax rate. There is absolutely nothing about the loan that could actually produce tax savings for us, because it is a much higher tax regime in the US than it is in the UK.

Q271 Nick Smith: Does your US operation pay money to Holland and Switzerland?

Troy Alstead: It does not pay money to Holland and Switzerland. It does for coffee buying; not to Holland, but it buys its coffee from Switzerland, yes. All our global coffee comes through Switzerland—everywhere in the world—whether it is to independent licensees or to all our company-owned structures round the world.

Again, I think the important point here is that we have \$200 million of royalty payments coming from totally independent companies around the world—unrelated to Starbucks entirely, but paying that same 6% royalty—which pay the same price for the coffee. It is extremely validated by all the analytics—the benchmarks and comparisons—as well as the fact that big, sophisticated companies are willing to pay that price for the value they get.

Q272 Nick Smith: Does the US pay 6%?

Troy Alstead: No, because the ultimate brand ownership of the company was rooted in the United States. That is where it was located.

Q273 Meg Hillier: In paragraph 6 of the information you sent us in advance, you talk about Lausanne being a global hub for commodity trading. Why is it that 75% of the world's coffee is traded through Switzerland? Is there a favourable tax rate for doing that?

Troy Alstead: Part of that is history. Long before Starbucks put our coffee buying in Switzerland, that was true. Yes, around coffee trading and trading houses in general, Switzerland offers a very competitive tax rate, which certainly complements that activity.

Q274 Meg Hillier: And then you charge 20% for selling it on to everybody else.

Troy Alstead: We must require to get cost and generate a profit whenever activities happen wherever they happen around the world. We always ensure that, wherever that profit sits, that is exactly where the activity happens.

Q275 Meg Hillier: And then you are paying less tax in Switzerland than if you did that, say, in London.

Troy Alstead: Yes. The Swiss tax rate has been approximately 12% over history.

Q276 Meg Hillier: What is your total tax payment in, say, the last financial year in Switzerland? Have you got that figure?

Troy Alstead: I do not have that with me. I am happy to provide that.

Q277 Meg Hillier: Could you provide that?

Troy Alstead: I am very happy to.

Q278 Meg Hillier: You talked earlier about your research and development costs. Presumably those get offset against tax, because they are then a dent in your profit margin. Is that right?

Troy Alstead: They would be tax-deductible costs in our business, yes, wherever they may occur.

Q279 Meg Hillier: Can you just remind us what the figure is that you spend on research and development to decide how to make a caramel macchiato or a frappuccino? What is your total cost for developing those products?

Troy Alstead: The number I quoted was approximately half a billion dollars a year, which includes not just product development—although that is a piece of it; for example, the frappuccinos and the Refresha products—but category development, marketing and brand development, the store design work we do, and the testing, engineering and certification of equipment. It is all the things that go into what we believe are very significant and important value-add businesses to make a store work successfully anywhere in the world. That is what that big category of spending is.

Q280 Meg Hillier: You spend a lot on that.

Troy Alstead: Yes, we do.

Q281 Meg Hillier: And that can obviously help you on the tax front. I won't run through the figures again, because colleagues have mentioned this, but if you look at what Costa or Caffè Nero earn and pay, they are also brands. In total numbers, I think that Costa comes top in the high street in the UK. It presumably spends money on research and development, but it still manages to pay tax. I am slightly puzzled. I wonder if you are paying more than other companies to make the Starbucks brand.

Troy Alstead: I can't speak about Costa, though I know they have been very successful here. Our intent is to make up that gap and be equally successful over time, and we have every intention of doing that.

Q282 Meg Hillier: How can you reassure us that the money you spend on research and development is genuine money and not inflated costs business to business within Starbucks for developing different ways of selling a cup of coffee?

Troy Alstead: The best way I can demonstrate that to you is by virtue of the fact—I am happy to provide this list to you afterwards if it is helpful—that all the large independent successful companies around the world recognise the value, so in a completely genuine arm's length transaction pay that 6% royalty. That is \$200 million a year paid by completely independent parties into Starbucks so that they can operate the business and keep the value.

Q283 Meg Hillier: But isn't that partly because your operating model is—or was—as I understand it, to buy up a lot of high street competitors, so you have several Starbucks on the same stretch of high street in busy parts of the city in London? You are not making

profit on them, but competitors are not there to buy the business. If you are setting up a coffee shop, your chance of setting up against Starbucks is limited. So, is it partly that people are paying because it is one way to be sure of keeping their coffee shop open? If you are with another company, you might get taken over or knocked out by the competition from Starbucks.

Troy Alstead: What you describe is part of our failed strategy in the UK. Many years ago we did go way too aggressive with opening sites on the high street and it was competitively driven. As I mentioned earlier, it is a very competitive marketplace here. We went too fast towards opening stores and we were willing to pay for high street locations that ultimately we could never make money on. Those, coincidentally, are now the stores that we have been closing.

We have closed more than 100 stores in the UK in the past 10 or 12 years. We announced a few weeks ago that unfortunately we have 22 more stores on which we have reached agreement with landlords. We need them, being exactly those high street landlords that we need to buy out of those lease commitments and close those operations. It is unfortunately a strategy—not by virtue of the wonderful partners, which is what we call employees who run the stores here—that is a legacy from the past when we opened stores that unfortunately will never make money for us.

Q284 Meg Hillier: You mentioned the Dutch tax arrangement that you have. You say that you have a confidential agreement with the Dutch tax authorities. Is that with the Dutch tax authorities or the Dutch Government?

Troy Alstead: It is part of the Dutch Government, so the Dutch tax authority. I fully appreciate that I have a responsibility to you, so I do want to provide that information. I am trying to find a way also to meet my obligations to them¹⁰.

Q285 Meg Hillier: I am not clear how the Dutch tax system works. In the UK, taxpayer confidentiality is important to our tax authorities—to HMRC—but you would be entitled to tell us that information. Are you saying that that is not the case in the Netherlands?

Troy Alstead: I feel bound by that relationship not to release it specifically. That is what we have been communicated.

Meg Hillier: It looks a bit cosy from the perspective of the British taxpayer.

Q286 Chair: Is it a sweetheart deal that you don't want to reveal to us? Your chap is nodding behind. It is a sweetheart deal that you don't want to reveal to us.

Troy Alstead: I am fully prepared to give you that information, as I have said. I would rather not have it revealed publicly. That is what we have been asked to do. I will happily after this meeting provide it in writing to the Committee.

Q287 Meg Hillier: Chair, I think there might be some issues we should be raising with the Dutch Government.

Q288 Chair: Is it the Dutch authorities that said you could not reveal it?

¹⁰ Note by witness: see footnote 6

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Troy Alstead: They asked us to hold that in confidence over time.

Q289 Chair: Okay. I want to intervene with one question. The whole point of buying in Switzerland is to save money for the business, isn't it?

Troy Alstead: No, that is not the whole reason. Global coffee buying happened there long before we got there. If we were going to trade coffee it had to be in Switzerland.

Q290 Chair: Okay. You say in your thing to us that you buy there because of major economies of scale—you save money. You say that in paragraph 6. "We achieve major economies of scale from centralising this activity."

Troy Alstead: That could be anywhere in terms of economies of scale. It is in Switzerland—

Q291 Chair: But you say that is what you do?

Troy Alstead: Yes.

Q292 Chair: Is that what you do?

Troy Alstead: We do all global buying in one place, in Switzerland.

Q293 Chair: So why don't you pass that on to your wholly owned subsidiaries? Why do you charge them 20%? Why don't you just pass that on, if for any other reason than what it looks like to us—you are avoiding tax? In Switzerland you have a lower tax regime. Where are you taxed in Switzerland, which canton?

Troy Alstead: Vaud—

Q294 Chair: What is it there? 2%, 3%, 4%, what is it?

Troy Alstead: It is a 12% tax rate.

Q295 Chair: 12%—less than the 24% here.

Troy Alstead: Yes, it is.

Q296 Chair: So why don't you let the UK coffee houses have the advantages of the economies of the scale and sell the beans to them at price, at the price you get?

Troy Alstead: We must generate a profit in every location around the world—

Q297 Chair: Why?

Troy Alstead: Because the Swiss tax authorities will require that we pay a tax on those inter-company activities. Just as if we generated income in the UK, we have tax obligations.

Q298 Ian Swales: That is where I wanted to come in. You were talking about the operation in Switzerland, and you said earlier that you make 7% or 8% profit on that. Is that on the cost of the operation in Switzerland, or is that on the turnover of the operation in Switzerland?

Troy Alstead: That is on the turnover—the sales of that operation.

Q299 Ian Swales: So an organisation of 30 people, which buys and sells these beans, makes 7% or 8% profit on its sales, just for commodity trading. Yes? It must be an incredibly profitable activity.

Troy Alstead: It is not just commodity trading, although that a key part of that activity. It is also all the coffee certifications around the world, the sustainability programmes, the agronomy offices that we have located in the growing regions—

Q300 Ian Swales: I am sure you are not going to tell me, but I am guessing that the net profit on that would be absolutely enormous. Do you know of another

commodity trading activity in the world that makes that kind of profit, simply on buying and selling?

Troy Alstead: I do not have benchmarks on other companies, but we are very prepared to provide that information to you.

Q301 Ian Swales: They sell this all to Holland, the entire—Sorry, do they buy for anyone else besides Starbucks?

Troy Alstead: No, just for Starbucks.

Q302 Ian Swales: Just for Starbucks. And then they sell everything they buy straight to Holland, is that right?

Troy Alstead: No, we sell to all our manufacturing geographies around the world; Holland is simply one of them.

Q303 Ian Swales: Is it only the UK or only the European use that goes through Holland?

Troy Alstead: The European use goes through our Amsterdam manufacturing operation in the Netherlands.

Q304 Ian Swales: In Amsterdam. So the US operations, for example, they get theirs direct from Switzerland.

Troy Alstead: Yes.

Q305 Ian Swales: Do they pay the same price as Amsterdam?

Troy Alstead: Yes.

Q306 Ian Swales: Okay. Then the Amsterdam operation presumably puts a mark-up on before it sells to the UK. Is that the same mark-up to every country?

Troy Alstead: Yes it is. It is the same price whether it is company-owned or licensed within the EMEA region for us.

Q307 Ian Swales: And are you able to say—forget the European headquarters—what the profitability of the roasting operation is? You gave us a figure for the buying, what about the roasting?

Troy Alstead: Again, the mark-up effectively—the profit on the sales of that coffee—is approximately at 20% gross margin.

Q308 Ian Swales: Is that 20% on top of the 7% or 8%?

Troy Alstead: No, that is all in.

Ian Swales: Altogether, okay.

Troy Alstead: The 20% is not net profit, that is the gross profit, and then we do have the expenses of running the operation as well, so it generates lower profitability ultimately.

Q309 Ian Swales: So you have to pay for the buying and the roasting out of that 20%, are you saying?

Troy Alstead: The 20% is the gross profit that sits on the sales of the coffee.

Q310 Ian Swales: Are your franchisees or licensees free to buy anybody else's coffee?

Troy Alstead: No. If they operate a Starbucks coffee shop, they must buy Starbucks coffee. That is what makes it a Starbucks coffee shop.

Q311 Ian Swales: So you can charge them whatever you like really.

Troy Alstead: No, because they would never agree to that if that was the case.

Q312 Ian Swales: Okay. How has it moved over time, and how does it move? Has this 20% gone up, down or stayed the same?

Troy Alstead: It has stayed the same over time. It is a cost plus, so if green coffee costs rise, it will move up or down over time, but the percentage margin has been very stable.

Q313 Ian Swales: So it is directly related to the market price for coffee. Is it the market price as quoted in the press or whatever, or is it what you actually pay in Switzerland?

Troy Alstead: It is what Starbucks actually pays for the various coffees we buy in the growing regions around the world.

Q314 Ian Swales: And whatever that price is, that is how the cost plus is calculated.

Troy Alstead: Ultimately, yes.

Q315 Ian Swales: I know from my own background, transfer pricing is the best way to do this, not royalty payments, so I am just guessing that there is something in this transfer pricing area.

Troy Alstead: Transfer pricing is how the coffee moves all around the world. That is a separate item from the royalty, which is the goods and services around the Starbucks store, the branding and the product innovation.

Ian Swales: I understand.

Q316 Fiona Mactaggart: How much do you pay in tax on the money that is remitted to the US?

Troy Alstead: Our average US tax rate is approximately 38%.

Q317 Fiona Mactaggart: Right. And you said to us that you spent 16% tax on royalties, half of which was in the Netherlands and half of which was in the US. That seems to me as though you are paying not just a very low percent in the Netherlands, but nothing.

Troy Alstead: No, we are paying tax but it is a very low tax ruling.

Q318 Fiona Mactaggart: Would you provide the Committee with both the amount of tax—if you have to do that privately, I am sure that the Chair would accept it—and evidence that the Dutch authorities have formally requested you not to reveal it?

Troy Alstead: I can consult and see what we can provide to you. I am very happy to be as transparent as I can about that relationship. I assure you that in our relationship over the years, they have very much wanted us to be confidential in our discussions.

Q319 Fiona Mactaggart: I am interested in what you have said about the number of people whom you employ in Switzerland and the Netherlands. As I recall, it was a few hundred, compared with 8,500 people here in Britain, and yet you are paying tax in those places and not here. That, you will understand, is one of the reasons why people find the structure of your company strange. You are certainly generating activity, which enables these profits down the line, here in coffee shops in Britain. You say you are shutting 22 of them because they are not profitable, but 22 out of 700 does not seem very significant to me. You can understand, can't you, why we feel that this is arranged in order to push the profits into places other than the places where the sales are generated that actually make the profits possible down the line?

Troy Alstead: I do understand. Again, we pay £25 million to £35 million of tax every year in the UK. We have not, unfortunately, paid the income tax, although we fully intend to. We have to get this

business into profitability. We have challenges with our property costs, challenges that are reflective of high costs in the market but also of our own failings over time with our real estate strategy. It is 15 percentage points of turnover higher here than our benchmarks in the US, for example. That is fundamentally why we have had such a challenge making money in this market.

Q320 Fiona Mactaggart: What is the difference in the price of a cup of coffee here and in the US?

Troy Alstead: It is probably approximately 20% higher on average, I would say. It depends on the market, because it is not a flat price.

Q321 Fiona Mactaggart: Exactly. So it is 15% higher in property costs, and it is 20% higher to pay for a cup of coffee. It seems to me that you are covering those additional costs in the cost of your coffee.

Troy Alstead: No, actually the percentage of property costs is on the higher price, so it is that much more relative to the two and half points even than what I said, but just as a percentage of turnover, which captures the higher price of the beverages here, it is extremely costly on our P and L. It is something we are working to fix, but we just have not been successful at fixing the financial model yet.

Q322 Stephen Barclay: What is the tax rate you pay in Switzerland?

Troy Alstead: Approximately 12%.

Q323 Stephen Barclay: Is there a Swiss ruling on that, or is that the standard rate?

Troy Alstead: My understanding is that that is a much more common rate that is provided to trading houses. I do not think it is a special ruling.

Q324 Jackie Doyle-Price: Earlier on, you said that one of the reasons why you were in the UK and you were prepared to tolerate these losses was that you had to be in the UK to be recognisable as a global brand. You have kept referring over and over again to the competition in the UK marketplace. Is it a fair characterisation of your position that Starbucks is willing to take short-term losses for long-term establishment as the global leading player?

Troy Alstead: Partially, yes. We are prepared to commit to the long term here. We have every intention that we must make long-term profitability. We have not yet; I appreciate that and I fully understand why the question is there; but absolutely we are prepared to invest to build our business over the long term. Every time we start a market around the world, they usually lose money for a short period of time to begin with, but nowhere near as long as here. That has been our challenge and our failing, historically.

Q325 Jackie Doyle-Price: The reason why this concerns me is that it looks very much to me like you are manipulating your tax affairs in order to support very aggressive anti-competitive behaviour. You have referred repeatedly to the issues with your real estate, but we see in a report in the *FT* that that was one of the consequences of the degree to which you were outbidding Coffee Republic for commercial sites. The figures speak for themselves: Coffee Republic now has a mere handful of stores compared with Starbucks, which is growing. That leaves me in a very uncomfortable position, both as a consumer and as a

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taxpayer. We in Britain are very concerned about fair play, and one of the reasons why we have embraced Starbucks is because of your emphasis on fair trade and your emphasis on ethics. Do you really think this will help you build the position that you want, both as a global player and as a main player in Britain?

Troy Alstead: I can assure you that we are not trying to outbid coffee shops today. Yes, five and 10 years ago, as we were rapidly growing in this marketplace, but we had no intention to be outbidding somebody as much as we had an intention to build our presence on the high street. That led us to pay often very high rates—often unsustainably high rates, unfortunately—but not intentionally: we believed at the time we signed those stores that they would become profitable for us. It has become clear over time that many of them will and many of them will not. We have since then really refined our strategy to recognise that the high-priced, long-lease prime real estate sites may not be the best strategy here, and we have to be much more diversified throughout the country. That is how we have modified our strategy over time, but yes, we did make those real estate mistakes—not conscious decisions, but mistakes—in those early days.

Q326 Jackie Doyle-Price: I was looking at your website earlier today, and you have got some very positive statements about the ethics of your company. Would you consider making a commitment to the British marketplace about the degree to which you will have a fair approach to taxation here?

Troy Alstead: Very much so. I assure you that we have every intention to be a fair taxpayer everywhere we are. We are never aggressive in avoiding taxes by any means. As I said earlier, we do not have tax havens in place; that is just not how we do business. We look forward to deepening our investment in this marketplace. We have every intention to do that.

Q327 Chair: We look forward to it too, Mr Alstead, after 15 years when you have not. Before we move on to Amazon, what we have got out of this is that in Switzerland you charge 20% profits on every coffee being bought in the UK, where you only pay 12% tax. You have not been able to explain to us the 6% royalty in any meaningful way. You charge for loans to your wholly owned subsidiaries at least 2% above the going rate. It seems to us that you are exporting your profits to minimise your tax. It does not surprise me that the YouGov brand index, which used to have a three-point positive, now has a 26-point negative. Are you happy with that?

Troy Alstead: No. We are not happy with it at all.

Q328 Chair: Let's move on to Amazon, and then we will come back to some general questions at the end. Amazon, when I buy a book from you—I do it online, and I am a regular buyer—I get amazon.co.uk. That is what I am told. Is that correct? I can show you. In fact, I think you write to me every day with new offers. It is from amazon.co.uk. Do you accept that?

Andrew Cecil: Chair, maybe I can explain how we are set up as a single European company, because I think that is very useful background for the Committee.

Q329 Chair: Let me ask you my questions, because I am asking from a UK perspective. It is the UK where we seek the taxes in these troubling times, and we

want everybody to give their fair share—all in it together. I just want you to explain it to me. I buy from amazon.co.uk—that is where I buy from.

Andrew Cecil: Amazon.co.uk is the trading name for Amazon EU Sarl, and we operate—

Q330 Chair: But you are saying to me that this is a UK company that I am buying from.

Andrew Cecil: No, you are purchasing from a single European company. We operate a single European company.

Q331 Chair: But it says to me—I'll show it to you—amazon.co.uk. Is that actually to lie to me about the origins of your company?

Andrew Cecil: Not at all. Maybe for the Committee's benefit I can explain how we manage our business—

Q332 Chair: No, I just want to pursue this issue, because I think I am buying from a British company. That is what I think when I get an e-mail from you or when you advertise. I think I am buying from a British company. I then agree to purchase something and I get an e-mail from you telling me that it is being delivered from a UK warehouse. That is correct, too?

Andrew Cecil: Yes, we have eight warehouses in the UK.

Q333 Chair: And I am told how much I am going to have to pay for the Royal Mail to deliver the books, or the toys, or the kettles to my home.

Andrew Cecil: Chair, if I may, it may be that it is delivered from a fulfilment centre in the UK, but could it actually be—excuse me, warehouse. We use the term “fulfilment centre”.

Q334 Chair: No, because I am always asked to pay the UK Royal Mail postage. That is what I get on my bill.

Andrew Cecil: You will be charged the postage as a UK customer, but actually we may be delivering that product from any of our in excess of 20 fulfilment centres across Europe.

Q335 Chair: I can tell you that they always come to me with a UK postage stamp on them. I am a regular purchaser of books, toys, kettles and so on, and there is always a UK stamp.

Andrew Cecil: Again, if I could explain, we run a single European business—

Q336 Chair: I believe I am dealing with a UK company; it comes to me via the Royal Mail with a UK stamp on it. That is what happens, and I tell you again that I have been purchasing from you—so far; I may change my mind—regularly in that way. When did any book that I purchased ever get to Luxembourg?

Andrew Cecil: We do not have—

Q337 Chair: Do you have books in Luxembourg?

Andrew Cecil: No, we do not have a fulfilment centre in Luxembourg. We have our European headquarters in Luxembourg, and as a single—

Q338 Chair: But the books are here?

Andrew Cecil: The books could be in the UK; they could be in France. If you are purchasing books in English, it is very likely that they will be in our fulfilment centres in the UK.

Q339 Chair: Thank you. I wish I could say that I am fluent in other languages, but on the whole I purchase books in English. So I buy from, I think, a UK

company; I am billed by the UK company; I am billed from the UK—

Andrew Cecil: No, I think you will see that Amazon.co.uk is a trading name for a Luxembourg company, Amazon EU Sarl.

Q340 Chair: I am billed from the UK. I can tell you, that is where it comes from. My bill comes from the UK. Do you want to see one of my bills? I have got them here.

Andrew Cecil: I can assure you, Chair, that you will be billed by a Luxembourg company, albeit we will be applying—

Q341 Chair: So are you telling me that the bills are printed in Luxembourg?

Andrew Cecil: The bills themselves may be printed in one of our fulfilment centres; that is one of the services—

Q342 Meg Hillier: When you say fulfilment, you mean one of your warehouses?

Andrew Cecil: Yes. Apologies, I thought I had sorted that out.

Q343 Chair: So the bills are printed in the warehouses, which on the whole, because I buy English books, are in the UK, and I think I am buying from a UK company. What business is conducted in Luxembourg?

Andrew Cecil: In Luxembourg we have our European headquarters. To give the Committee a sense, we have in excess of 500 people working there. In fact, we are still recruiting very heavily and we expect to add another 100 people to our headquarters in Luxembourg—

Q344 Chair: And how many people do you have in the UK?

Andrew Cecil: Across the UK today, we have about 15,000 employees.

Q345 Chair: The figure we have got is 2,265, to be absolutely precise. That is the figure for people employed here.

Andrew Cecil: If I may, I would like to correct that, Chair. We have in excess of 15,000 people working—

Q346 Chair: 15,000?

Andrew Cecil: Yes.

Chair: My goodness.

Andrew Cecil: If I may continue, Chair, we have just announced that we are actually hiring an extra 10,000 seasonal employees to help us with Christmas.

Chair: Okay—

Andrew Cecil: If I may finish, I have just one final point. Just in September, while we were opening our new warehouse in Hemel Hempstead, we announced that we would be hiring also an extra 2,000 people over the next 12 to 24 months.

Q347 Chair: We are delighted that you are have business in the UK. I was delighted that I thought I was buying from a UK company, which delivered, from a UK warehouse, books that have never appeared in any other jurisdiction. Why are you not paying tax in the UK?

Andrew Cecil: We do pay tax in the UK—

Q348 Chair: Why aren't you paying corporation tax in the UK?

Andrew Cecil: We pay corporation tax in the UK.

Q349 Chair: How much do you pay in corporation tax? 0.2% is the figure I have got, I think—or something like that.

Andrew Cecil: I am happy to say that the accounts of our UK company, Amazon.co.uk Ltd, are publically filed. For 2011, we had revenues of £207 million; we made an after-tax profit of £1.2 million and we recorded a tax expense of £1.8 million.

Q350 Ian Swales: Can we follow the Chair's paper chase a bit further? Clearly, she is has the understandable perception that she is buying from the UK. Can you talk about the invoicing: how that works, how the money flows, and how the money then flows back to the UK for delivery and so on? What are the actual arrangements?

Andrew Cecil: If I may, what I was trying to do at the outset was explain that we are operating a single European company, which is I think to your point. That company is our retail business across Europe, known as Amazon EU Sarl. That is a pan-European business: we have five websites across Europe; we are serving tens of millions of customers across the whole of Europe, as well as sellers. That is our principal trading company in Europe. The accounts for that company are publicly available in Luxembourg, and I am very happy talk to those accounts.

Q351 Ian Swales: So when the Chair buys her book, the money comes to Luxembourg and you essentially pay a small amount back to the UK to have it delivered. Is that correct?

Andrew Cecil: The company we have in the UK, Amazon.co.uk Ltd, is a service company for group companies including our Luxembourg European headquarters.

Q352 Ian Swales: How is Amazon.co.uk Ltd? What is its income? How does it get its income?

Andrew Cecil: As I mentioned, these are publicly available. They are filed in Companies House. So for 2011, the turnover of Amazon.co.uk Ltd was £207 million. We—

Q353 Ian Swales: From doing what? How did it get £207 million?

Andrew Cecil: That is essentially for providing services in the UK for the Amazon Europe companies—services such as operating the fulfilment centres, which is going to be receiving inventory, picking, packing and then passing on those products to our—

Q354 Chair: How much is declared in Luxembourg of sales into the UK?

Andrew Cecil: To the point, as a European company, what we file in our accounts are our Europe-wide revenues. For 2011, we had Europe-wide revenues of €9.1 billion. If I may, I will give the Committee some other data points there. We made a profit after tax of €20 million on those sales.

Q355 Chair: €20 million on €9 billion?

Andrew Cecil: Yes.

Q356 Chair: Can you answer my question? Out of the €9 billion—it looks like a peanuts profit, so presumably that was all exported to some tax haven.

Andrew Cecil: No, not at all.

Q357 Chair: Oh. Where did it go then?

Andrew Cecil: That is the profit that we make on what—

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Q358 Chair: Say it again? On €9-point-what billion, how much did you make?

Andrew Cecil: Chair, maybe just to give you a parallel, I can talk to our worldwide figures for 2011. Our worldwide—

Q359 Chair: No, don't befuddle us with that. We really care about the UK, because we think you are not paying the right tax in the UK. What I am interested in is how much of your Luxembourg business is sales into the UK.

Andrew Cecil: Unfortunately, we have never broken out revenue figures on a country or website basis.

Q360 Ian Swales: You must be joking. Come on, you can't be serious.

Andrew Cecil: We operate a pan-European business. Those are the only figures we have ever broken out.

Q361 Ian Swales: I used to be a finance director of a pan-European business. If somebody asked me, "What do you sell in each country?" I would be fired immediately if I did not have the answer to the question. That's ridiculous.

Andrew Cecil: Those are numbers that we have never disclosed publicly.

Q362 Ian Swales: Will you disclose them privately?

Andrew Cecil: I am very happy, should the Committee wish, to come back and see whether it is possible to disclose them privately to the Committee.

Ian Swales: That is totally evasive.

Q363 Mr Jackson: Did you say that you do not know the sales and revenue in each jurisdiction, or that you do not want to tell the world?

Andrew Cecil: What I said was that we have never publicly disclosed any sales figures for those jurisdictions.

Q364 Mr Jackson: So you do know. You, for instance, make a cost-benefit analysis as to whether it is worth your while investing in capital—say, building a new warehouse at Milton Keynes or wherever. You have a business case for each individual jurisdiction—each region.

Andrew Cecil: We would certainly have a business case for making a large investment, such as investing in building a new fulfilment centre. We are currently looking to build three new fulfilment centres in the UK, and obviously we present a very specific business case on each of those fulfilment centres.

Q365 Mr Jackson: Okay, can I come back from Mr Swales's questions? I am fascinated by this idea that this entity in Switzerland, which in 2010 employed 134 as opposed to 15,000 in the UK, is the engine room of this business, in terms of value and tax liability. What about payroll? Where is the centre of activity in terms of finance and payroll?

Andrew Cecil: If I may just correct that, it is in Luxembourg, not Switzerland.

Mr Jackson: I beg your pardon—Luxembourg.

Andrew Cecil: And it is not 134. We are in excess of 500 people today, and we are hiring.

Q366 Mr Jackson: Okay, 500, as opposed to 15,000. Where is finance and payroll for the UK business?

Andrew Cecil: All the strategic functions for our business in Europe are based in Luxembourg. That could be our retail business, our third-party business, our transportation teams, our customer service, HR, finance—

Q367 Mr Jackson: But where is finance and payroll for your UK operations? Where is human resources and web design for your UK operations?

Andrew Cecil: Maybe I can come to that. Working for Amazon.co.uk Ltd, we also have people looking at those issues supporting the European company.

Q368 Mr Jackson: That is a very circuitous answer to a straightforward question. We are following a sort of audit trail here with a book. The book is billed from the UK; it is packed from the UK; it is bought in the UK from a domain name that ends with .co.uk. We are talking about the value added to the business: is it in the UK or is it overseas? And I am asking you: are the support functions for that business in the UK?

Andrew Cecil: The employees of the UK entity are basically working for Amazon.co.uk, and they are being rewarded for that in the revenue figures of the UK company.

Q369 Mr Jackson: So, if I'm Joe Bloggs and I want a job driving a forklift truck at the Milton Keynes warehouse, who interviews me, who processes my application form, and who ticks my diversity form to get a job with you? Is it in Europe, or is it in the UK?

Andrew Cecil: I am not familiar with the details of that, but I can certainly find out exactly how it would work. I don't know how that would be for a specific applicant.

Q370 Mr Bacon: You don't know?

Q371 Chair: If you employ someone in the UK, do you go through the recruitment process in the UK or in Luxembourg?

Andrew Cecil: If you are working for the UK company, you would clearly go through the recruitment process with the UK company.

Q372 Mr Jackson: And who pays those people in terms of their monthly salary?

Andrew Cecil: That is paid by the UK company.

Q373 Mr Jackson: Okay, so we've got recruitment, payroll, finance and HR all in the UK.

Andrew Cecil: I don't think that is a fair representation. On a Europe-wide basis, all these functions are led by people who are physically based in Luxembourg, working for the UK company.

Q374 Mr Jackson: But they don't go for the job interview in Luxembourg, do they? If you are driving a forklift truck and shifting books in Peterborough or Milton Keynes, in the warehouse—

Andrew Cecil: You would be going for the job interview with the UK limited company, because that would be who your employer would be.

Q375 Mr Jackson: Which leads one to believe that that is where, essentially, the core activity is, in generating the wealth.

Andrew Cecil: No, I disagree, again. We are operating as a pan-European business so, for example, that person working in the fulfilment centre in the UK might actually be shipping products that are purchased off our French website by a customer in Belgium. It is very important for the Committee to understand that that is how we operate as a business.

Q376 Mr Bacon: You have already said that if they are buying an English book in English in the UK, it is most likely that that will be fulfilled from a UK warehouse. Presumably the same is true for a French

book in French published by a French publisher and sold in France to a French buyer, isn't it?

Andrew Cecil: There are two points I would make. When Madam Chair ordered her book on Amazon, one of the things we were obviously keen to do was to deliver it to her as quickly as possible, so for English books, we stock many of them in our fulfilment centres in the UK, exactly so that we can offer same-day delivery to our customers—

Q377 Mr Bacon: I think we all understand that if you tried to fulfil for Mrs Hodge from your fulfilment centre in Tierra del Fuego, it would take a lot longer. What we are really trying to get at, and I think what Mr Jackson is trying to get at is: where is the underlying economic activity, the components of which create what we all know as added value and which eventually creates value added tax—or would it weren't books. It seems from your answers that the answers to those questions are, "in the UK." You said that the people who work in the UK are employed by Amazon.co.uk Ltd, and they are paid by that company, presumably with money that that company has in the UK. Is that correct?

Andrew Cecil: It is revenues that that company makes.

Q378 Mr Bacon: In the UK?

Andrew Cecil: No, let me make it clear. The revenues, for example, from Madam Chair's purchase of the book are revenues that accrue to Amazon EU Sarl, not to the UK company.

Q379 Mr Bacon: If I am Mr Jackson's forklift truck driver in Milton Keynes and I am working each month and I get paid my salary at the end of the month, that money goes into my British bank account. Where does it come from? Does it come from a British bank account, controlled by Amazon? Yes or no?

Andrew Cecil: I can confirm to the Committee, but I am almost certain it will come from Amazon.co.uk Ltd.

Q380 Mr Bacon: So does it come from a British bank account controlled by Amazon?

Andrew Cecil: Yes.

Q381 Mr Bacon: So it is not the case that the people in Luxembourg have to wire over some money each month to pay this chap's salary. It is sitting in a UK bank account controlled by Amazon and that is where the money originates—starts its journey—that ends up in the forklift trucker's bank account?

Andrew Cecil: Amazon.co.uk is a service company in the UK providing services to Amazon EU Sarl for which it receives payment.

Q382 Chair: The Comptroller and Auditor General will ask some questions now.

Amyas Morse: Just a couple of quick questions. The quite low turnover in the UK is because the way you have it set up is that the UK company provides services and its customer is the European company for those services. Is that right?

Andrew Cecil: One of the group.

Amyas Morse: Okay. They send their invoice to Luxembourg and get paid and that is where the money that goes into the bank account more or less comes from. They do not have ownership in the books?

Q383 Chair: I pay in pounds, actually.

Amyas Morse: I know. I am just trying to get bank details. So the services that this UK company is doing are essentially handling services. They don't actually own the book at any point.

Andrew Cecil: No, the UK company does not own the inventory.

Amyas Morse: I am only saying that for clarity. Now, my second point, if I may bring you back—I am sorry—because I heard the discussion, is that you know perfectly well what sales are happening everywhere in Europe, otherwise you couldn't possibly run this company, the advertising or anything else, so if you are not giving that information it is because you choose not to. That is right, isn't it?

Andrew Cecil: No. Let me stress, we are operating on a pan-European basis—

Amyas Morse: But you know the information. You cannot possibly pretend—and it is really quite annoying to listen to—that you can possibly be running a strategy in Europe and not know your territorial profitability. You are doing advertising. You are putting up warehouses on the assumption of sales volume. Come on, it is actually quite insulting to everybody's intelligence to say that you don't know what sales volumes are going to be in the territory. That is just not feasible as an argument. You cannot possibly advance that. I don't think anyone who knows anything about business would accept that line.

Andrew Cecil: As I said previously, it is not numbers that we do disclose but I am very happy to go back to the company and see whether we are willing to—

Q384 Stephen Barclay: Can I just check that you are telling the C&AG that you don't disclose country-specific data to the SEC? In your filings to the SEC you don't put, for example, what UK earnings would be?

Andrew Cecil: I am not aware that we have that in our ICC filings.

Q385 Chair: What we are getting at in these conversations is that your entire economic activity is here in the UK. I even pay in pounds—it never comes off my bank account in euros. Your entire activity is here, yet you pay no tax here, and that really riles us. It riles us.

Andrew Cecil: Can I clarify? We do pay corporation tax. Our accounts for Amazon.co.uk are—

Q386 Chair: A tiny bit in relation to—you won't tell us your sales. A tiny bit.

Andrew Cecil: The other thing I would also highlight is that we have paid in excess of £100 million in payroll taxes in the last five years. We have paid tens of millions in business rates in the past five years.

Q387 Chair: I have heard this argument before. Let me just kill this argument because it really makes me cross. On the one hand, so does every other business. The community-based bookshop that you are putting out of business also pays business rates, also pays its PAYE, and probably pays VAT in a way that you don't. You are making it uncompetitive. The other thing is that you depend on the services that come out of the tax you pay: you depend on the ability to get your goods around, so you have to get the roads in place—you depend on all those things. Probably worst of all, you and Mr Alstead employ people on, probably, minimum wage, if we are lucky, and then

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we, the taxpayer, pick up the tax credit bill for that too. We are putting a lot of money back into the people you employ, and you are not putting enough tax back into our economy. That is what is riling us all. Sorry, I shouldn't have done that. Austin.

Q388 Austin Mitchell: No, I thought that was quite good. I have to say, Mr Cecil, I am a satisfied customer. I love the service you provide when you write to me and say, "Having bought this biography of John Major, you may also be interested in 'Fifty Shades of Grey'." But like the Chair, I am interested in why you pay so little tax—particularly corporation tax—in this country. If you paid more, we could pay some kind of benefit to all the booksellers you have put out of business. Undoubtedly, you have put a large number of booksellers, including some local ones in my area, out of business.

I do not get from this interview why Luxembourg is so lucky—the books are here, the warehouses are here, the billing is here, the business is here and the customers are here. There are, on our figures, 134 staff in Luxembourg, and 2,266 in the UK. According to Richard Murphy of Tax Research UK, in 2010, £122.8 million of profit was generated in the UK, and £2.2 million in Luxembourg, but you pay tax in Luxembourg and not here. I put it to you that that is really because you can offset a lot more costs against tax in Luxembourg. In 2010, the figures seem to show that £7.56 billion of profits were offset against £7.4 billion of charges, so, effectively, you were escaping pretty well scot-free in Luxembourg. That is why you're there, isn't it? That is why we have all this business about favouring Luxembourg.

Andrew Cecil: May I address the various points one by one? First, I would like again to refute that we are putting booksellers out of business. What we are seeing is that the internet retail industry is bringing huge benefits to consumers across Europe in terms of price, in terms of selection and in terms of convenience, and we are very much focused on continuing to invest to make sure that consumers can benefit from internet retail.

On the figures you quoted, I really do not know where they have come from, so I cannot comment on that. As I said earlier, our accounts, both for Amazon.co.uk Ltd and Amazon EU Sarl are publicly available. I would be very happy to provide the Committee with a copy of those. I would like to confirm that we do pay corporation tax in the UK, and we also pay corporation tax on any profits we make for Amazon EU Sarl. I think that covers most of the points. I do not know whether I have missed any.

Q389 Stephen Barclay: Who owns the Luxembourg company?

Andrew Cecil: Luxembourg is owned by a holding company, which is a subsidiary of our group companies.

Q390 Stephen Barclay: Where is that located?

Andrew Cecil: The holding company is also in Luxembourg.

Q391 Stephen Barclay: It is also in Luxembourg. That seems a slightly artificial arrangement, doesn't it?

Andrew Cecil: I am not familiar with the details of the holding company, but I would be very happy to come back to the Committee.

Q392 Stephen Barclay: So what is the effective tax rate that you pay in Luxembourg?

Andrew Cecil: Worldwide—I have the figures here—

Q393 Stephen Barclay: No, in Luxembourg.

Andrew Cecil: I would need a calculator. I apologise. For 2011, our net profit after tax was €20 million, on revenues of €9.1 billion.

Q394 Stephen Barclay: Sorry, can you just say that again? In Luxembourg, your profit was €20 million.

Andrew Cecil: Our revenues across Europe for 2011 for Amazon EU Sarl were €9.1 billion. Our profit after tax was €20 million. The tax expense—

Q395 Nick Smith: Did you say that your profit after tax was €20 million?

Andrew Cecil: Maybe to that point, I would point out that we are investing very significantly not just in the UK but across Europe, which may be reflected in these numbers.

Q396 Stephen Barclay: Do you have preferred equity certificates, then, in Luxembourg?

Andrew Cecil: I wouldn't know. I am very happy to find out and come back to you. Maybe I can finish on the point that the tax we paid—and this is a tax expense recorded on our accounts for 2011—

Q397 Stephen Barclay: What I am interested in is how you are stripping out the profits in Luxembourg, because that is the impression. If it is €9.1 billion going to €20 million that suggests that you are stripping out the profit in Luxembourg. Who owns the holding company?

Andrew Cecil: I will need to come back to the Committee on that.

Q398 Stephen Barclay: So the profit is going into a company, and is then going to a holding company. What about the title and goods from affiliates or third parties—

Q399 Ian Swales: Sorry, that is another unacceptable answer. You are telling us you don't know the corporate structure of your company. Really?

Andrew Cecil: I do know the corporate structure of the European company. I work for the European company. I would be happy to come back.

Ian Swales: All we need to know is who owns the holding company.

Q400 Mr Bacon: You are the director of public policy. It is incredible that you wouldn't know who owns the holding company. It is just not credible.

Andrew Cecil: I am very happy to come back to the Committee.

Mr Bacon: Well, you can tell that we are not happy.

Q401 Chair: Do you know who owns it?

Andrew Cecil: No. I will come back to the Committee with an answer.

Q402 Chair: Do you know who owns it?

Andrew Cecil: No, I personally do not know—

Q403 Chair: Do you know who owns it?

Andrew Cecil: No, I don't.

Q404 Stephen Barclay: But it is where the money goes, isn't it?

Q405 Chair: Isn't there someone behind you? Haven't you brought advisers with you?

Q406 Stephen Barclay: Well, we have probably got another 40 minutes or an hour to go. I am sure one of your advisers could go and make a call, and come back to us in 10 or 15 minutes, with the Chair's permission, with the answer. It can't be too difficult to phone head office and find out who owns it, can it, Mr Cecil?

Andrew Cecil: I will certainly provide that information to the Committee.

Q407 Stephen Barclay: So we can have that before we close today? That would be useful. What I am interested in, really, is where the profit is going and how it has been stripped out. Can we look at it in a different way, through title and goods from third parties and affiliates—can you talk through how that is handled?

Andrew Cecil: Again, I am not quite sure what you are specifically talking about. It is very clear what our revenues are, what our profits are and what tax expense we have accounted for across Europe. The inventory of goods that are in our fulfilment centres across Europe belongs to Amazon EU Sarl and does not belong to the local entities that we may have across Europe.

Q408 Stephen Barclay: So why is the UK not a branch?

Andrew Cecil: I am not a detailed tax expert on that question, but again I would be very happy to come back to you.

Stephen Barclay: Because it is a tax issue—it is not a business issue. It is about getting the structure of the tax bill.

Q409 Nick Smith: Let me ask this question again. Of the €9.1 billion of European sales in 2011, what were your sales in the UK in 2011?

Andrew Cecil: If I may, I will give the same reply to the Committee—I will come back to the Committee and if it is possible to disclose that figure I will disclose it.

Q410 Mr Bacon: Could you say that again?

Andrew Cecil: I will come back to the Committee. I will see whether it is possible to disclose that figure. We have not disclosed those figures, ever, publicly, either on a country basis or a website basis.

Q411 Stephen Barclay: Why is it so confidential what your earnings are by country? I might be missing something, being a generalist, but what is the secret that pertains to country-by-country data?

Andrew Cecil: This is how we have disclosed our financial data over a number of years now. We have never broken out revenues on a country basis.

Q412 Chair: What are you hiding?

Andrew Cecil: We are not hiding anything, Chair. As I said, I am very happy to come back to the Chair on a confidential basis and see whether it is possible to disclose that.

Q413 Nick Smith: That, Mr Cecil, is the most ridiculous answer I have heard in months and months on this Committee. That is just pathetic. Of the €9.1 billion sales you made in 2011, you have said that you made €20 million after tax. What did you make before tax?

Andrew Cecil: I would assume—again, I don't have the figures—that, as we had a tax expense that was

around €8 million, that we made a profit of the two combined. But I would need to check.

Q414 Nick Smith: So you made a profit of €30 million on revenue of €9 billion? Is that what you are saying?

Andrew Cecil: No, what I am saying is we made an after-tax profit of €20 million on that specifically.

Q415 Nick Smith: What was your profit before tax?

Andrew Cecil: Before tax—I do not have that specific number there, but I am happy to provide it to the Committee.

Q416 Chair: Mr Cecil, you don't have anything. Honestly, you have come to us with absolutely no information. What is your job?

Andrew Cecil: I am director of public policy for Amazon across Europe.

Q417 Chair: Well, I think what we are going to have to do is order somebody to come who can give us answers to the questions we ask. We will order somebody to appear before us who does that. It is just not acceptable. I don't know what you take us for, but we need proper answers to perfectly proper questions, which are trying to establish the economic activity in this country, and therefore what would be a reasonable corporation tax due. That is our job. The idea that you come here and simply do not answer the questions, and pretend ignorance, is just not on. It is awful.

Andrew Cecil: Chair, I am very happy to provide the Committee with any responses to these questions.

Q418 Chair: No. I cannot believe you have come without the information—or they have deliberately sent you. We will order somebody who can answer the questions, in public.

Q419 Stephen Barclay: What do you publish regarding the holding company? What data do you publish?

Andrew Cecil: Again, I would have to come back.

Q420 Stephen Barclay: That is where the money is going. The money is going from one Luxembourg company into the holding company, and what we want to try to get visibility on is the flow of money from that company into the holding company. It does seem remarkable you do not know who owns it, or how much money it is getting.

Andrew Cecil: I don't have it in front of me, but I will make sure that we provide those to you.

Chair: Dear, dear. Well, we will have to come back to this. I am just going to go through colleagues, quickly, and then we will go to Google, and then we have got some general questions. Fiona and Ian, you can have a chance.

Q421 Fiona Mactaggart: Mr Cecil, one of the things I am struck by, here, is that you have a lot of satisfied customers, who are not trying to do Amazon down. It is in my constituency—what I thought was the headquarters of the company, which allegedly is in Luxembourg, but nevertheless; when I have been taken round by Brian McBride, and his successor, Christopher North, I was not told that this is a Luxembourg-based company. I was told, "Here we are, developing lots of products." It did not sound to me like an operation which ran fulfilment centres—i.e. warehouses—all round Britain. It sounded to me like a company which was kind of being grown here,

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which got its ideas here, which made the bulk of its sales here. Are you saying that they misled me?

Andrew Cecil: I was not with Mr McBride. I am sure Brian would never have misled you. As I said, we are operating on a single European company basis. We do have Amazon.co.uk Ltd, which operates the fulfilment centres, and obviously in your constituency we have our corporate headquarters for the UK. We are delighted to be there, and employ hundreds of people.

Q422 Fiona Mactaggart: Do you understand why we think, particularly when we are not able to get detailed answers from you, that a company which has 30 times as many employees in the UK as in the place where it is allegedly headquartered, which developed itself in the UK—I remember when the first picking centre was in Slough—and which developed a growth in the UK which has outstripped, I think I am right in saying, other European markets: do you understand why we think that there is a deliberate structuring of the company to pretend that the UK is just an operation which is warehousing and sending, and not in any way an engine of this company? Do you understand why we are suspicious? Because we are—although we are happy customers.

Andrew Cecil: Again, let me make it very clear. The fact that we are running a pan-European business actually has huge benefits to customers, to sellers and to our suppliers. Let me give you a couple of examples. With a supplier, we will list their product; we will source from a pan-European basis. Rather than just list on the UK website we will list on all our websites—the UK website, the French website, the German website, the Italian website and the Spanish website. That is the way we are driving greater reach, greater sales—

Q423 Fiona Mactaggart: But you have just said to us that you cannot tell us how much sales each of those websites generate.

Andrew Cecil: Because customers can shop off any of those websites. They don't need to shop off the UK website.

Q424 Fiona Mactaggart: Absolutely. I understand that; and when I am buying Christmas presents for my relatives in America I shop off the American website. I completely understand that; but each website must know what profits it returns, or what sales it returns, because frankly we think that you manipulate your profits, and that they are a separate thing to your sales. You do not seem to be able to tell us either what sales each website returns or what profits each website returns. Those are two questions that, had I been coming before this Committee, I would have known the answer to.

Q425 Chair: Mr Cecil, I think you are not serious—they have sent you up as a sort of I don't know what. You are not serious here.

Andrew Cecil: Not at all.

Mr Bacon: That's right, not at all.

Andrew Cecil: I mean, I disagree with you, Chair.

Q426 Chair: It is outrageous. We are a very busy Committee but we will ensure that you answer. First, we want an answer to the question—

Andrew Cecil: I will provide answers to all the questions.

Chair: No, we want an answer this afternoon to the question about the holding company. Secondly, we will expect a serious person to appear before us. We will order them, and do that as soon as we can after recess, probably on a Thursday morning. Right, now Google. Sorry, did you want a go, Ian? I just do not think you will get anything out of it.

Q427 Ian Swales: I might not, but it will be interesting to hear. One area we have not touched on at all so far is VAT. There is no VAT on books, but Amazon sells plenty of other things and it is killing lots of retailers in other fields—we have just seen Comet go under—so can you tell me what VAT I pay if I buy an electrical item from Amazon? What rate of VAT?

Andrew Cecil: Let me address the point about our competitors. We strongly believe that internet retail is highly beneficial to consumers.

Q428 Ian Swales: I am not against internet retail, by the way, it is whether it is a level playing field.

Andrew Cecil: On consumer electronics products, which was your question, for a sale to a customer in the UK we apply the standard UK VAT rate, and that would be collected on behalf of the UK Government.

Q429 Ian Swales: Even though I am buying from a Luxembourg company. So how was it that two weeks ago you were pulled up for selling online books and only charging 3% VAT? Even though you were charging British publishers 20% VAT, you were then only charging 3% VAT—you were using the Luxembourg tax rate to sell those. Is that something you do across other product lines, or was this a one-off?

Andrew Cecil: I think you are referring to consumer electronics versus e-books. For e-books—

Q430 Ian Swales: I am talking about VAT.

Andrew Cecil: Yes, the VAT applicable to consumer electronics versus e-books. For e-books, by law we are required to apply the Luxembourg VAT rate on e-books, because we are a Luxembourg-based company—which we do, which is 3% VAT.

Q431 Ian Swales: So anyone in the UK selling e-books who has to charge 20% has a massive disadvantage against yourselves.

Andrew Cecil: We think e-books is a very nascent, growing market segment—it is highly, highly competitive. There are many providers, both of devices and of content, out there—

Q432 Ian Swales: How did you feel about the EU ruling that said you had to increase it, that Luxembourg was not allowed to do this any more? It has been given 30 days to increase the rate to 15%. How do you feel about that?

Andrew Cecil: I cannot comment on a ruling of the Commission. I think that what we would say is that, from our perspective, we firmly—

Q433 Chair: By November you have to decide whether you are going to challenge it. Are you challenging that ruling?

Andrew Cecil: Sorry, Chair, I do not think that we are challenging the ruling, Amazon is not a party to these proceedings. What I would say is that we firmly believe that a book is a book, regardless of—

Q434 Ian Swales: The one thing you are in charge of—it is obviously not finance—is public policy, but

you do not know whether you are going to challenge an EU ruling. Is that not a public policy matter?

Andrew Cecil: I do not think that you can challenge such an EU ruling—I am not aware that that is actually possible.

Q435 Chair: Are you being investigated, by the way? Is Amazon being investigated in a number of jurisdictions, as we speak? Your tax affairs?

Andrew Cecil: We are audited—very standard practice—in a whole range of jurisdictions—

Q436 Chair: Are you being investigated in the USA?

Andrew Cecil: No, I cannot comment on specifics.

Q437 Chair: You cannot comment, or you are or you are not?

Andrew Cecil: As I said, we are regularly audited in a number of jurisdictions—

Q438 Chair: Are you being investigated—that is my question—in the USA?

Andrew Cecil: I cannot comment on any specific investigations.

Chair: You do not know—

Andrew Cecil: No, I cannot comment—

Q439 Chair: Are you being investigated in China?

Andrew Cecil: I cannot comment. I am sorry, Chair, I am not very familiar with—

Q440 Chair: You are public policy, you might know this: are you being investigated in China?

Andrew Cecil: I am not aware of any investigations against us in China.

Q441 Chair: Are you sure that is the truth?

Andrew Cecil: Personally, I am not aware—

Q442 Chair: Are you being investigated in Germany?

Andrew Cecil: I am not aware of any investigations in Germany.

Q443 Chair: Are you being investigated in France?

Andrew Cecil: We have publicly declared in our most recent findings that we have received an assessment from the French tax authorities and we dispute that assessment.

Q444 Chair: You are. In Japan?

Andrew Cecil: I am not aware of whether that is so, personally.

Q445 Chair: In Luxembourg?

Andrew Cecil: No, not as far as I am aware.

Q446 Chair: Okay. Let's move on to Google. Mr Brittin, what is your job?

Matt Brittin: I am vice-president for Google in northern and central Europe, which comprises the wetter countries of Europe.

Q447 Chair: That includes the UK?

Matt Brittin: Yes, most definitely.

Q448 Chair: I have found the Google situation most difficult. I have had to create drawings for myself to understand how the Google intra-company system works. As I understand it, 92% of all sales outside the USA are billed in Ireland. Is that right?

Matt Brittin: I am not sure if it is 92% but the vast majority of sales outside the US will be billed in Google in Ireland. That is correct.

Q449 Chair: Why?

Matt Brittin: First, let me say that we pay the tax we are required to pay in every country in which we operate, including the UK.

Q450 Chair: Well, it depends where you choose to put the business, doesn't it? That is what this

afternoon is all about. It depends where you choose to put the business.

Matt Brittin: Given that we are talking here not about a business that makes money from its consumers but about ones that makes money from business-to-business advertising, perhaps I can quickly talk about how Google is set up.

Q451 Chair: People do that to avoid the questions actually.

Matt Brittin: Certainly not.

Q452 Chair: It seems to me that we have Google UK, which acts as an agent to Google Ireland Ltd, if you look at my little picture.

Matt Brittin: I can't see your drawing.

Q453 Chair: It doesn't matter but it is about that. Google UK acts as an agent for Google Ireland Ltd. Corporation tax in Ireland is 12.5%. Is that right; am I correct?

Matt Brittin: I will try to answer your first question first. When Google became popular outside the US, we set up in Ireland to serve the whole of the European Union under the single European market.

Q454 Chair: Why Ireland?

Matt Brittin: We chose Ireland for a range of reasons, one being that it has a competitive rate of corporation tax. We pay 12.5% there. Other reasons include a skilled labour force in technology; Microsoft, Oracle and others were there. Property and other costs for our staff are also lower than, for example, in central London. Ireland is the base of our operations for Europe. It has data centres and we have invested tens of millions of euros in space, equipment and people in Ireland. Everybody who buys advertising from Google—because that is how we make our money—buys advertising from Google in Ireland. That is in just the same way as any company can set up to trade within Europe.

Q455 Chair: Okay, I understand that; thank you for that clear answer. Google Ireland Ltd pays a fee to Google Netherlands Holdings BV.

Matt Brittin: Shall I talk about Google UK, which was your second question, and then I can come to the rest of it? In the UK, Google has a business, Google Ltd. It had a revenue last year of £396 million and we paid corporation tax of £6 million on that business. It made an accounting profit of £31 million. So we pay corporation tax in the UK. Over the past three years that business has grown significantly as we are a relatively young business, so we have grown. What the people in the UK do is provide services that are charged to Google Ireland. Those services are principally around promoting our products and making sure they work in the UK for UK consumers. What is different about Google versus the other businesses you have been talking about, is that we are not selling books or making coffee.

Q456 Chair: You're selling advertising space.

Matt Brittin: For the services we provide, the consumers are based on the computer science that drives search and other technology such as Google Maps and so on. That is all done in California: clearly, innovations that have never been seen in the world before, in terms of computer science that allows you to search the internet.

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Q457 Mr Jackson: But the UK adverts are specific to UK search engines, aren't they?

Matt Brittin: Yes. Perhaps I can explain briefly how it works. If you are a consumer in the UK—a mother in Merseyside looking for a birthday present for a daughter—you search for cool bags on Google UK site. It is a UK site in that the content you see is more focused on the UK than if you were searching on the global site. You might find an advertisement in there, one of the blue links that says ads from the Cambridge Satchel Company. That would be one of our customers and that customer would pay only if you were to click on the link and go through to the site that, in that case, is trying to sell you a satchel.

That allows people on the business side to target people who are searching on google.co.uk or Google France or Google US or any other geography against particular words. The advertiser pays only when a consumer clicks on what they have chosen to do. One reason for operating in Ireland is that many of our customers in the UK want to reach consumers all around the world, and in Ireland we have more than 3,000 people speaking 50 different languages, and helping businesses in Europe to connect with consumers in Europe and across the world. That is why we are organised in that way.

Q458 Chair: But the ad that you see in the UK—this is an important point because it is back to trying to see the economic activity in the UK—is different from the ad you would see in the Netherlands.

Matt Brittin: If you were the Cambridge Satchel Company, selling satchels, and you chose to target someone who types in “satchels” in the Netherlands, they would see an ad for those satchels in the Netherlands.

Q459 Chair: But you sell UK-specific advertising space, which will be seen by all of us.

Matt Brittin: Yes, it is possible for any company, anywhere in the world to advertise to a UK user—

Q460 Chair: Do you have people in the UK selling your advertising space?

Matt Brittin: Anybody who buys advertising from us in Europe buys from Google in Ireland from our expert team—

Q461 Chair: Where are they based? Do they go door to door, knocking? Presumably there is a marketing sales team that goes round trying to sell advertising. Where is it based—in Ireland?

Matt Brittin: It is an internet-based business, so most of our customers transact online or on the telephone with experts in Ireland. We have people in the UK. For the accounting year I mentioned—the last year we filed—we had 1,300 people in the UK, and that is now up to about 1,500.

Q462 Chair: Who sell advertising space in the UK.

Matt Brittin: They do a range of things promoting our products. Some of them work with businesses, because businesses want to be educated by Google about the internet and its opportunities. Businesses can use a range of things from Google, including free tools. Google Analytics is one that helps people to understand how their website works. If they want to buy advertising from us—they are encouraged to do so by our people in the UK—they will buy it from our expert team in Dublin.

Q463 Chair: Can you answer this? Of your 1,200 people, was it, in the UK—

Matt Brittin: There were 1,300 last year, and more now.

Chair: How many are in the sales force, and marketing?

Matt Brittin: Nobody is selling or promoting the products, but they are definitely encouraging people to spend money on Google. No one is buying from them.

Q464 Chair: Who is selling into the UK market? Who is doing the selling? Who is trying to encourage people to advertise on your search engine?

Matt Brittin: There are people in the UK—

Q465 Chair: Doing that. How many?

Matt Brittin: Of the 1,300 last year, I think about 700 were marketing and digital consultancy people, and some of those, but only some, were working with customers.

Q466 Chair: How many are selling from Ireland into the UK? How much money?

Matt Brittin: We have 3,000 people in Ireland. They do a range of different things.

Q467 Chair: How many are selling from Ireland into the UK?

Matt Brittin: A couple of hundred—something of that order.

Q468 Chair: So 700 in the UK and a couple of hundred in Ireland.

Matt Brittin: But the 700 in the UK include people who do things like make all the consumer products work—maps and everything else that has to work in the UK market.

Q469 Chair: So there is economic activity.

Matt Brittin: But the bigger thing here is that all the technology that creates the economic value, and all the innovation that powers Google search, comes out of California.

Q470 Chair: This is your loyalty stuff. I am coming to that.

Matt Brittin: No, it is not loyalty, Madam Chairman.

Q471 Chair: I am trying to get where the economic activity is.

Matt Brittin: I am just trying to explain that.

Q472 Chair: You very helpfully told us that about 700 people sell into the UK—marketing people—compared with 200 in Ireland. What I do not understand is that the Irish guys pay a fee to Google Netherlands Holdings BV. Is that to save withholding tax?

Matt Brittin: There was an arrangement in place to do that, but I understand that it is no longer necessary.

Q473 Chair: But was it put in place to save withholding tax?

Matt Brittin: That is my understanding.

Q474 Chair: It was. Thank you. That is a very direct answer, and the first we have had today. But it is no longer necessary. Does it therefore go to Google Ireland Holdings?

Matt Brittin: That is correct.

Q475 Chair: Which is registered in Ireland but administered from Bermuda.

Matt Brittin: That is correct.

Q476 Chair: So if that happens, your profits go to Bermuda. How much is sitting in Bermuda?

Matt Brittin: I do not know the number, but it is true that Bermuda is part of our operations, and the reason is that when an international company sets up operations outside your domestic market, which in our case is the US, you look for where to locate your operations. Within the European Union, we chose to locate in Ireland, for the reasons I have explained, but you also need to protect your intellectual property, and to set up operations in countries around the world to do that. We have an entity in Bermuda to do that.

Q477 Chair: What I appreciate is that you have openly told us that you chose Ireland and then Bermuda because they are both low-tax, if not no-tax.

Matt Brittin: That is right. As a multi-national company, we have a duty—

Q478 Chair: What really gets the UK ordinary punter out there who uses Google day in, day out is that they contribute to your business. There is economic activity—I use Google, and all of us round the table use Google. They contribute to your profits but see no proper, fair contribution from you to corporation tax. That is the thing that bugs us all.

Matt Brittin: I understand, but I think it is a misunderstanding. We pay corporation tax here—

Chair: A tiny bit.

Matt Brittin: May I try to answer? We pay corporation tax here on the activity that our people here do. But, if you think about Google, it is technology. The 17,000 engineers in California who build and continue to invest in developing the technology create the economic value for Google.

Q479 Chair: What does Bermuda create?

Matt Brittin: Let me explain. What creates economic value for Google is the technology and the computer science. Hopefully, people understand that, because it is pretty magical to be able to search the entire web in seconds and get answers fast. That is what we continue to invest in.

Q480 Chair: So, what does Bermuda create?

Matt Brittin: Let me just explain. So, that is how we create the economic value. Tax law suggests that you need to pay tax where the economic value is created, and we believe that that is there. In the case of the economic activity in the UK, which is about helping people to understand how to use the internet and products and services, we have looked at how best to establish what we should pay for the services that are provided by people in the UK. The way we come to a conclusion on that is, if we went outside and hired other firms to do those kinds of things, what would we pay there? That is how we have set up our cost structure.

Q481 Chair: What does Bermuda create?

Matt Brittin: In Bermuda, we have an entity that holds the rights to our intellectual property, and you can tell it is a very intellectual property business—

Q482 Chair: But I thought you just told us that the intellectual property is all in California?

Matt Brittin: I was trying to finish the sentence, which is, the intellectual property rights for outside of the US, for the licence—

Q483 Chair: But the research and development is all in California.

Matt Brittin: That is right, but we, like any company, are required to do two things. One is to play by the

rules, and when you set up internationally, you need to make decisions about how to protect your intellectual property and how to organise. Secondly, we are required to manage our costs efficiently in order to satisfy our shareholders. And our goal as a company is to—

Q484 Chair: So you are minimising your tax even though it is unfair to British taxpayers.

Matt Brittin: It is not unfair to British taxpayers. We pay all the tax you require us to pay in the UK. We paid £6 million of tax last year—

Q485 Chair: We are not accusing you of being illegal; we are accusing you of being immoral.

Matt Brittin: It is not a matter of personal choice.

Q486 Stephen Barclay: In terms of your US filings, do you do what tax accountants refer to as check the box?

Matt Brittin: I am afraid that I am not a tax accountant. My job is to run the business in Europe—

Q487 Stephen Barclay: But it goes to the heart of how passive income is dealt with, doesn't it? Because the Bermuda operation is dealing with your intellectual property rights outside the US—that is correct, isn't it?

Matt Brittin: Yes.

Q488 Stephen Barclay: And, as you also said, this is a US company.

Matt Brittin: Google Inc. is a US company, that is correct.

Q489 Stephen Barclay: And, like you, I am not an expert in tax affairs—far from it—but as I understand it, there are rules in the US in terms of the treatment of income earned by a US group outside of the US, are there not?

Matt Brittin: I am sure there are. I am not an expert. I focus on the UK and Europe—

Q490 Stephen Barclay: Again, like with Mr Cecil, it goes to the heart of the issue, because, if I understand it correctly, what we have is a choice of location in Ireland because there is a low corporation rate—the Chair alluded to a debate about to what extent business is done in Ireland and to what extent it is done in the UK—but then there is the more interesting question about what happens to the money from Ireland. As I understand it, that is going to Bermuda, and the question in my mind is why is that not being captured from a US tax perspective? The phrase that was suggested to me is that there is a way, in terms of US filings, that one can get around this, which is referred to as “checking the box”, hence my question.

Matt Brittin: I am not familiar with the phrase you mention. I can assure the Committee that the tax that we pay in the UK, and how we operate in Europe, has nothing to do with those arrangements outside. The tax we pay in the UK is a function of the activity that people do in the UK that is in line with UK law, and the way we operate around the world is in line with the law in every jurisdiction in which Google operates.

Q491 Stephen Barclay: No one is suggesting that you do not operate in—the CAG has expertise on this, so he may want to come in. Amyas?

Amyas Morse: Thank you. I only wanted to say that I have some familiarity with Bermuda, and I am sure that it is a good place to protect intellectual property

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rights, but the primary reason that people locate companies in Bermuda is because it is a low-tax area—that is right, isn't it? So what you are doing is rolling up royalties in Bermuda, a protected tax zone. That is not illegal, but the fact is, if I compare this to the discussion we had with Starbucks, they said that, in their tax policy, they do not use offshore tax havens but you do; that is part of your strategy. I am just pointing out that it is somewhat different. That is fine. So you are rolling up money in Bermuda. Do you remit that by dividend to the UK or are you just piling it up in Bermuda?

Matt Brittin: No. The tax we pay in the UK is a function of the activity that we do in the UK and our accounts are published—

Amyas Morse: I know, but I am asking about Bermuda.

Matt Brittin: Absolutely. All I can say is that the tax that we pay in the UK is nothing to do with affairs of Bermuda or anything else. It is entirely influenced by the way we set up in Europe, with one centre in Ireland to serve everybody. The activities that we do in the UK—similar to other countries in Europe that are not Ireland—are similarly compensated and structured, so the people on the ground are helping people make the most of the web and the people in Ireland are helping to operate the systems and sell advertising to the businesses that want to work with us. That is how operations are set up, and that is personally what I focus on.

Q492 Chair: Mr Brittin, you have been really helpful and I appreciate that, but this session was about tax. I think you knew that before you came, so it is slightly odd—again—that we have got a witness who does not understand tax. Have you got people behind you who do?

Matt Brittin: I was personally requested, by name, to come to the Committee.

Q493 Chair: Were you? Not by us.

Matt Brittin: You did. You asked for me personally and I actually had to reschedule, because I was in Germany and so I came especially for this.

Q494 Chair: Okay. Can we just get an answer to this question that I think Stephen asked: are there any check-the-box elections made below Bermuda for IRS purposes?

Matt Brittin: For the third time, I don't know what that phrase means. I'm sorry; I'm not a tax expert and I don't focus on the US. What I can do is find out and share with you afterwards. That's all I can do.

Q495 Stephen Barclay: In essence, it's the revenue that's coming in to Bermuda and how that is being treated from a tax perspective.

Matt Brittin: I will happily answer, but I will have to have someone else do it for me.

Q496 Ian Swales: I was quite amused, actually, that the first briefing that I looked at for this meeting had an ad by Google and it was, "Take home 90% of your pay", which turned out to be a complicated tax avoidance scheme for IT contractors. But you've only made money advertising a tax avoidance scheme there.

Matt Brittin: Only if you click it.

Q497 Ian Swales: My real question is that we think of Google a lot when we think about search engines,

but I know—because I have been personally lobbied a few times by Google—about it trying to get more into public sector provision of computing. I know that you have already set a toe in the water with—is it Hertfordshire county council, or one of the councils in that area? Can you talk us through that process? If a public sector organisation in the UK actually contracted with Google for the provision of computing services, how would the revenue be booked, what cost would be booked against it and therefore what tax would be payable?

Matt Brittin: The vast majority of our revenue globally comes from advertising rather than from the kind of computing services that you talked about; in excess of 90% of our revenue, I believe, comes from advertising. However, we have a small but growing business providing things like e-mail, document production and collaboration software. That is small. It is similar to the Gmail service, and so on, that consumers have.

Q498 Ian Swales: In the lobbying, I am told that the whole of Los Angeles and I think the whole of San Francisco run their IT on your platforms, and the sales pitch is that they would like lots of the UK public sector to do the same thing. So clearly this is a drive for you.

Matt Brittin: It is a small but growing business, and lots of companies and some local authorities are using those services. It is not an entire IT solution; it is the Gmail that you are used to as a consumer.

Q499 Ian Swales: What I am really interested in is this: suppose that a public sector organisation contracts with you for a certain amount of revenue. What cost will be put against that revenue before a profit is struck on which tax is payable?

Matt Brittin: That is not a core part of our UK business, but I imagine—

Q500 Ian Swales: Is it a part of it? Have I been lobbied by some ghosts? Is it a part of your UK business or not?

Matt Brittin: It is part of what our teams in the UK would do, and it is a relatively small part. There would be a handful of people in the UK who would be focusing on encouraging customers to use—

Q501 Ian Swales: I have met this "handful" and I am asking, "What happens if I do business with them?"

Matt Brittin: When you do business with those guys, I think the revenue and costs would be similar to the way that the advertising business is structured in the UK. I will confirm if that is incorrect, because it is a small part of the business. The innovation that drives the economic value of that business comes from our teams in California in the US, who are building and developing products—in this case, Gmail and other associated products—for use by millions of consumers and, increasingly, millions of businesses. So that would work in a similar way.

Our view would be that the economic activity—the innovation, the computer science that drives that—is in the US and therefore, rightly, the majority of the profit and the tax should be in the US.

Q502 Ian Swales: So would it be a good approximation to say that whatever profit is made on that service would effectively end up in Bermuda and, possibly, the US? Therefore, should the UK public

sector factor that in when it is thinking about who to do business with—whether it is going to get tax back or not? Would that be a thing that we ought to think about?

Matt Brittin: The UK public sector benefits from competition, including Google, and can select whatever products and services it wants to use. We think that ours are good and that they work well, and they are chosen by a range of people, but anybody buying software and services should make their own choices on these things. But it is the case that the people we have in the UK, the UK Ltd business we have in the UK, pay tax, and it pays all other taxes that it is required to do. We look at whether that is an appropriate amount based on what we would pay if we did not have that business but had to outsource to third parties—that is how we arrive at the numbers that we pay in the UK.

Q503 Ian Swales: One last question from me. You are the UK chief executive, are you?

Matt Brittin: No, as I said at the beginning, my job is vice-president for operations across northern Europe.

Q504 Ian Swales: Yes, the wetter countries, I remember now. Where are you based?

Matt Brittin: I live in London, but I spend my time around all of those countries.

Q505 Ian Swales: Where are you paid?

Matt Brittin: I am paid in my bank account in the UK.

Q506 Ian Swales: And are you an employee of Google UK, or what?

Matt Brittin: I think I am, because I live here and, until a year ago, I was running our business in the UK.

Q507 Ian Swales: Do you get any compensation from any other part of the world?

Matt Brittin: My compensation comes through my payroll and so on, which comes from here, but I am paid—my bonus and so forth—as an executive of Google Inc. globally, so my compensation is based on the company's overall performance as a—

Q508 Ian Swales: Via the UK PAYE system.

Matt Brittin: We pay it however it is paid—yes.

Q509 Mr Jackson: Mr Brittin, can I just ask you about if you had a more orthodox structure between the UK company and Ireland, with a proper disaggregated business model, and a different pricing structure. To an extent, from what I see in the last two years, on a turnover of £600 million you have made losses in both financial years, which suggests that your pricing structure is wrong at the very least. But if you had to pay tax on profits, would that persuade you to leave the UK?

Matt Brittin: First, can I correct what you said? In the last two years we have paid tax because we have earned an accounting profit—

Q510 Chair: Tiny. Tiny in relation to your turnover and tiny in relation to the UK business. What is the UK business?

Matt Brittin: I will tell you the numbers again, if I may. In 2011—

Q511 Mr Jackson: You have paid £8 million in corporation tax in six years on a £6,000 million turnover in revenues—in the six years to 2010. That is not exactly pushing the boat out for the taxpayer, is it?

Matt Brittin: I do not quite recognise the figures you have said there. Last year, the revenues in the UK were £396 million, we made an accounting profit of £31 million and we paid tax at 26% on that accounting profit, which is £6 million in tax.

Chair: Mr Brittin, we are not naive. The revenues in the UK are those that you choose to put through the UK. What we are interested in is the actual revenues you earned in the UK.

Q512 Mr Jackson: For the avoidance of doubt, the figures that I have—you are of course free to challenge them if you wish—are a loss of £6.1 million in 2011 and, for corporation tax purposes, a loss of £0.9 million for 2010.

Matt Brittin: No, those are not the figures I have. I will happily give you a written submission on the figures. There is an issue in that we pay tax on an accounting profit; we are then required to deduct stock-based compensation, so the statutory number that goes into Companies House would be a loss, but actually we paid tax on £31 million-worth of profit, which is £6 million on a tax rate of 26%. That is on a revenue of £396 million which, as I explained, we think is appropriate because that is about the amount we would have had to pay if we had gone to third parties and asked them to do the same services. The people in the UK are not doing the innovation, they are not doing the computer science, they are not doing the product development—

Q513 Mr Jackson: What are they doing?

Matt Brittin: As I explained, they are working to help consumers and businesses to get the most out of the internet. The point here is not about sales—

Q514 Mr Jackson: No, come back to my specific question, if we may, because we can meander along different paths—

Matt Brittin: I am trying not to meander, I apologise.

Mr Jackson: Were you to adopt a more robust business model in which, God forbid, you are making a profit—

Matt Brittin: We are making a profit, and we are paying tax.

Q515 Mr Jackson: In the UK—a real profit, rather than just part of a tax avoidance scheme, which it clearly is.

Matt Brittin: No, I have to say, we are paying the tax that we are required to under law, and we are not avoiding tax.

Chair: You are avoiding tax—within the law.

Q516 Mr Jackson: I think you are avoiding tax. My question is: would you leave? If you had to pay a higher rate of tax on a decent profit—which this is not—and you left, where would you go?

Matt Brittin: I think that the issue of your understanding here is this: if Google was a British business—if it had been founded in Cambridge by Larry and Sergey—I think we would be in a very different place here, because the profitability rightly would sit with where all the technology and innovation happened. But Google is not a British business. Google is a US business. With any activity that happens in the UK, even if you were to describe it as sales activity, which is not exactly what the people do, we could still go and get that activity from

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the open market at the kind of costs that we are paying to the UK Ltd business.

Q517 Chair: But the profits from your UK activity end up in the Cayman Islands—in Bermuda, sorry.

Matt Brittin: Regardless of where any profits end up, the business in the UK—

Chair: But that's where they end up. That is what is so irritating.

Q518 Mr Jackson: So the shareholders in Google UK cannot access that cash. What is the market capitalisation of the company in Bermuda? Do you know?

Matt Brittin: We do not have a market caps on our traded company. Google has a market caps, and that is Google Inc., which is an American company, as you know.

Q519 Mr Jackson: My point is that if you buy shares in the UK company you are not necessarily going to be able to easily access—

Matt Brittin: You can't buy shares in the UK company because it is a wholly owned company. You can buy shares in Google Inc., which is an American company.

Mr Jackson: Okay, an American company.

Matt Brittin: Yes, you can buy shares in Google Inc. and participate as a shareholder.

Q520 Mr Jackson: Can you just finish answering the question about where you would go? Are you basically saying that if the tax take was higher it would not be viable for you to continue to operate in the UK?

Matt Brittin: No. What I am saying is that we pay the tax required in every company in every country in which we operate. Every country—every Government, just as you—has the right to set the tax rates they want to set, and every company has to decide how to organise. I hope I have tried to explain to you that the way we are set up reflects how our operations occur. I cannot comment on the hypothetical proposal. We run the business in a robust way. We think we do it in a way that is appropriate. It is certainly legal. We pay all the tax we are required to. We also have an obligation to shareholders, which is to ensure that we do that cost-effectively. We make choices, such as I have described, in order to make those two balances.

Q521 Fiona Mactaggart: Let's think about the interests of those shareholders. I am interested in what happens to the money that ends up in Bermuda, and how the shareholders can get any benefit from that. It seems to me that were that money to be transmitted to your shareholders you would have to pay tax on it, would you not?

Matt Brittin: Yes. As I say, the amount of tax we pay globally is a matter of public record and it is in the billions of dollars. The amount of tax we pay in the UK is a matter of public record and it was £6 million last year.

Chair: You are repeating yourself.

Matt Brittin: I am not clear about the question.

Q522 Fiona Mactaggart: What I am interested in is that it seems to me that you are developing a bank in Bermuda—a cash pile that adds to the capital gain in terms of your shareholders but which cannot be

remitted to your shareholders without their paying further tax on it.

Matt Brittin: I think that's a matter for our US organisation and the parent company. That is not something I am party to.

Q523 Fiona Mactaggart: Am I right in thinking that your tag line is “Do no evil”?

Matt Brittin: That is a phrase that is used to crystallise the values of Google and how we try to operate. Correct.

Q524 Fiona Mactaggart: It seems to me that, if I can just put it very gently, you are not matching up to that. If you rack up cash in Bermuda, that means that, I don't know if you, but senior executives at Google will have lovely bonuses, which will be based on the surpluses made before tax, and yet your shareholders, whose interests you claim you are trying to protect by operating in low-tax regimes, can get no benefit from it.

Matt Brittin: I am not sure I understand fully the question. What I will say is, first, on “Do no evil,” we are proud to try to operate to a high standard. We might not always get it right, but what that means for us is offering an amazing service that allows you to search a trillion URLs on the web in a second on any device around the world, and that helps—

Q525 Chair: Not on tax, Mr Brittin. We are here to talk about tax.

Matt Brittin: As I have said, we pay all the tax required in every country in which we operate.

Chair: I understand that, but we don't think you pay a tax that is just.

Q526 Fiona Mactaggart: What we think you are is cleverer than the taxmen and taxwomen around the country, which is very good if you are saying, “We do no evil.” Okay, so you say, “It's in our interests to reduce our tax liability; that helps our shareholders.” I am trying to get you to answer what your shareholders get out of the money that you remit to Bermuda. It sounds to me like nothing.

Matt Brittin: As I say, I am not an expert on the way that operates, but what I would say is that we are required to pay tax on the basis of where the economic activity that is carried out that generates profit, and that is where our customers are—That is the guidance from the HMRC. What the HMRC says is that is not tax avoidance, but simply the way that corporation tax works, so we follow the way that corporation tax works internationally. I wish, as I said, that Google was a British business—we would then be having a different conversation—but the activity and innovation is in the US, which is appropriate.

Q527 Fiona Mactaggart: Could you perhaps provide the Committee with a note about how your shareholders benefit from the Bermuda holdings?

Matt Brittin: I am happy to do so if there is a specific question.

Q528 Chair: Before I bring in Meg, can I ask if you use other tax havens? Do you use the Channel Islands?

Matt Brittin: Not that I am aware of, but we do operate in a lot of countries around the world.

Q529 Chair: Bahamas?

Matt Brittin: What I will have to do is come back to you and let you know. If you have a list of places you want to check—

Q530 Chair: Cayman Islands?

Matt Brittin: My understanding is no, but I do not know for certain. Let me come back with a list. If you give me a list, we will tell you exactly where we operate.

Q531 Chair: Netherlands Antilles?

Matt Brittin: We have a business in the Netherlands, but not in Netherlands Antilles, as far as I know.

Meg Hillier: I think it is worth highlighting, and Fiona Mactaggart just touched on it about HMRC, that we are here to guard and follow the public pound—the tax pound—in the UK. I have to declare an interest in that I had a sandwich and a cup of coffee at the Google Campus only last week with the technology APPG group hosted there. Google does a lot of work to help and incubate new technology businesses, and that is really partly where we are driving. You have a structure that is set up in a way, as a modern internet business, quite differently from particularly the Starbucks business of selling a physical commodity; and one of our concerns is that our tax authorities are unable to pursue the money made in our tax jurisdiction in the UK for the benefit of UK taxpayers. You say that you wish that Google was a British business, but you are helping to incubate British and international businesses. Do you give them advice about tax affairs?

Matt Brittin: No, we do not give any businesses any advice on tax affairs. That is an important point you raise. You mentioned Campus: we invested in a building in the tech city area of London—a seven-storey building full of start-ups—and one of the things our founders are keen to do is encourage businesses to take advantage of the internet. The Committee may not be aware of this, but the UK is one of the leading markets in the world in terms of e-commerce. Lots of small businesses—we have 200,000—

Q532 Chair: That is why you make a lot of money out of us, Mr Brittin.

Matt Brittin: The point is that this is important for UK businesses. One of the big growth opportunities for the UK is the internet economy—

Q533 Chair: Absolutely. It is important for you too.

Matt Brittin: And we are part of the way in which those businesses reach consumers around the world. A business in Scotland selling kilts now has 70% of its sales outside Scotland, because every time somebody types “kilts” into Google, they can appear and they only pay when somebody clicks on the ad. We are very much part of that success story and business support. Businesses are happy to spend their money, because it is profitable.

Q534 Meg Hillier: Chair, the figure is dropping, but I learnt this interesting fact: 42% of people will only buy something off the internet if they can read about it in their own language. Although it is shrinking in its percentage, English is still the dominant language. Google, using English—America and the UK are, I suppose, the main English-speaking countries—is helping to drive that, and you could argue that is economic activity. There is an interesting question

about what economic activity is in the internet world. Where is it based? Where is the internet based?

Matt Brittin: Absolutely. You mention language, and one of the things we have developed as a free tool for consumers and businesses is Google Translate. I am not sure if people have used this, but it is actually getting quite good. It is a free tool and it allows a business that is selling to translate its website automatically into multiple other languages, which helps a UK business to export around the world. I go back to the point—

Q535 Meg Hillier: For balance, should I mention Lingo24?

Matt Brittin: Others are available on all these things. It is a free service. The key point here, as you think about the questions you are asking us, is where does the economic value come from? It comes from the computer science. Where does the computer science come from? It comes from 17,000 engineers in California who are building these things under the leadership of our team.

Q536 Chair: Not in Bermuda, Mr Brittin.

Matt Brittin: That is the economic success story for Google. I am proud to say that we are supporting thousands of start-ups now in the UK through our activity in tech city, but also through the fact that our paid advertising works in a way that no advertising has worked in the past, to help reach consumers around the world.

Chair: We are short of time, so have a quick go, Austin, and then we will go to some general questions for everybody.

Q537 Austin Mitchell: I would like a long go. One can hardly be surprised that you are going to opt for the softest tax regime possible. Our endeavour is to ensure that profits generated here are taxed here.

Matt Brittin: And they are.

Q538 Austin Mitchell: A couple of years back, I was told by ITV that Google now had bigger advertising revenue than ITV. I do not know whether that is still the case, but it is a fairly telling statistic. However, it was not paying the taxes that ITV—its competitor for advertising revenue—was paying.

Matt Brittin: That is a really good question, Mr Mitchell, in the sense that ITV is a commercial broadcaster, which generates all of its activity in the UK, and was granted a licence by the state for the spectrum it has.

Q539 Austin Mitchell: And produces programmes here.

Matt Brittin: And produces programmes in the UK. Google is a business that was built in America and continues to be an American business. All of the activity that develops our technology is led from, and the vast majority of the engineering is done in, America. That is the contrast. As I say, if Google was a British business, you would be looking at the profits being generated here, but Google is an American business and their profits are generated there, as HMRC advises and international tax law dictates. We do not have the opportunity to do anything else.

Q540 Austin Mitchell: I accept that, of course. I would want profits generated here by any business, whether it is a multinational or British, to be making a contribution to the Treasury.

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Matt Brittin: Of course, and we pay tax on the profits we make here.

Q541 Austin Mitchell: What we are trying to find out is where the money goes. Now, it goes to Ireland, it goes to Dublin. I could not make out from our Chair's somewhat incredible drawings—you couldn't see them, and I couldn't understand them, so we have got something in common to start with—whether it then goes to the Netherlands, which has lots of double tax agreements?

Matt Brittin: Any money that is spent by an advertiser in Europe—

Q542 Austin Mitchell: So it is not paying much tax in Ireland either.

Matt Brittin: Well, the tax rate in Ireland is 12.5%. There was an arrangement in the past, which I understand is no longer necessary, where there was an agreement via Google Netherlands. I understand that is no longer necessary. Think of the money being spent with Google Ireland. That money will go to pay some of the costs in Ireland—we have just opened a second data centre in Ireland.

Q543 Austin Mitchell: But it is not paying much tax, even if corporation tax is low. It is just passing through.

Matt Brittin: Correct. The corporation tax rate in Ireland is lower than it is in the UK.

Q544 Austin Mitchell: Yes, but you are still are not paying much of it.

Matt Brittin: The rate we are paying is 12.5% and the business is continuing to grow, so I expect over time we will make a bigger contribution, assuming that we will be successful.

Q545 Austin Mitchell: What cannot be fiddled through is paid at 12.5%, but the 12.5% is not paid on most of it. It then goes on to the Netherlands, and then it goes to Bermuda. Now, the interesting question is what that does for the shareholders. As Fiona said, it does not benefit them—they cannot get their hands on it because 30% tax would have to be paid for it to be repatriated to America, to the shareholders. It sits there in a cash mountain. It makes no contribution to all the research and development—the new technologies that you have been telling us about—that is carried on in California; it just sits there. It is probably lovely to visit it, walk round it, look at it, and think, “Ha ha ha,” but what contribution does it actually make?

Matt Brittin: It is a matter for the board of Google, but I imagine that, if the resources are needed to be used, they can be used.

Q546 Austin Mitchell: They couldn't be used in America because you would have to pay 30% tax.

Matt Brittin: They could be used in America if that were the case. Shareholders will benefit from the profits after tax that the company generates, and the company has choices about where it locates money over time.

Q547 Austin Mitchell: If Romney had got in, you would have been able to repatriate it to America, but he didn't get in, so it can't go back there.

Matt Brittin: There is no question there.

Q548 Chair: Amyas has a question.

Amyas Morse: It is a good argument about the activity based in California, but you keep on referring

to the fact that the income is actually generated from advertising.

Matt Brittin: That's correct.

Amyas Morse: That is not Californian advertising, is it? It is a slightly misleading argument, although I understand it. Of course, part of it is generated by the technology—that is the medium—but it is also generated by advertising and sales, which are specific to territory. So a significant part of the economic activity is specific to the territory; not all of it is global, that would not be fair, would it?

Matt Brittin: You are raising a fair point, and I want to be very clear on this. The economic activity that we carry out in the UK is paid for at what we believe is an appropriate rate, because we look at what we would have to pay if we went outside Google to get it. The advertising, though, just to be clear, is not the same as buying a double-page spread in *The Sunday Times*. It is a much more complicated, algorithmically-driven system that is almost as complicated as the system of search itself, because anybody can target any keyword, anywhere in the world, any phrase that is typed, across the multiple domains of Google. They can change their bids and the amount of text they say, which is complicated.

Amyas Morse: We are all users.

Matt Brittin: Okay, but it is very complicated compared with what you would traditionally view as advertising, and that is why we think it is appropriate, given that the technology that underpins the advertising, just like the technology that underpins search, is driven by engineers out of the US, where as I say we have 17,000 engineers.

Q549 Mr Bacon: Mr Brittin, you said you have £396 million of UK revenues, that is right isn't it?

Matt Brittin: That is correct.

Q550 Mr Bacon: I am trying to understand the costs of generating those revenues. The revenues are people paying for advertising, is that right?

Matt Brittin: No, the business in the UK is people providing services to Google Ireland, which is what I mentioned earlier, and they help consumers and enterprises to make the most of the web and encourage them to understand it. They run lots of sort of education on the business side—training to show them the kind of products that are available to use.

Q551 Mr Bacon: So the £396 million of revenue comes from Google Ireland.

Matt Brittin: It is paid by Google Ireland, that is correct.

Q552 Mr Bacon: All of it?

Matt Brittin: Yes.

Q553 Mr Bacon: In return for the provision of services.

Matt Brittin: Yes, and as I say, we determined that we think that is an appropriate amount based on looking at what we would have to pay to get similar people to do it in the market. So, for example, an agency or consultancy—

Q554 Mr Bacon: Actually, what you said was that it is determined on what it would cost if you went and bought the services from—

Matt Brittin: A consultancy firm or something like that.

Q555 Mr Bacon: Of course, if you have people in-house, they will generally be a lot cheaper than going out and buying it from a firm.

Matt Brittin: The reason we do it in-house is because we think this is all extremely new stuff and therefore the people in-house can understand in more detail the products we have, but it's a call: we could certainly hire a consulting firm or similar to do some of things that our people do. So that's how we try to judge that it is a fair amount.

Q556 Mr Bacon: It just strikes me as odd that the costs of generating this £396 million of revenue would be quite as high as it sounds they are.

Matt Brittin: That £396 million is the revenue earned by the UK operation, paid for by Ireland, and it is based on the costs of all the activity that we do here, plus a margin in order to reflect what we would pay in the open market.

Q557 Mr Bacon: Right, and you are selling those services to Google Ireland, which is paying for them, yes?

Matt Brittin: Correct.

Q558 Mr Bacon: Well, you said you had 1,300 employees in the UK?

Matt Brittin: Yes.

Q559 Mr Bacon: If you paid them £120,000 each, that would cost £156 million. That still leaves you with £240 million of other activity that Google Ireland would have to be paying for. I find it difficult to understand what Google Ireland is paying for that it is getting value for. I don't know if you are paying everyone £120,000 a year, but it just sounds very—

Matt Brittin: There are a bunch of other costs in there, including the cost of real estate. Our people are in two very big offices in central London and so on, so I am pretty confident that those are the costs that we pay out, because we would want to make sense of—

Q560 Mr Bacon: Sorry, what other costs?

Matt Brittin: The people and the real estate costs, and the other costs of having an operation of that size in the UK.

Q561 Mr Bacon: I am sorry, you said that you are pretty confident that those are the costs, I am asking what other costs?

Matt Brittin: On the £396 million, you've done a back of an envelope thing. I can share with you the accounts, which are published and audited every year, and the amount of revenue has gone up as the business has grown—I think the revenue line is double what it was three years ago, to give you an indication.

Q562 Mr Bacon: The revenue line from Google Ireland?

Matt Brittin: The revenue of Google UK Ltd, yes, which—

Q563 Mr Bacon: The revenue of Google UK Ltd paid from Google Ireland has tripled in the last—

Matt Brittin: It has more than doubled in the last three years.

Q564 Mr Bacon: So Google Ireland is paying you a lot more for a lot more services.

Matt Brittin: Yes, but don't forget that our business is growing pretty fast in the scheme of things as an internet business and is pretty popular.

Q565 Mr Bacon: Well if you are able to send the Committee a note detailing what those costs are we would be very grateful.

Matt Brittin: Certainly I can provide you a detail on that.

Q566 Stephen Barclay: Can I ask about the royalties you pay from Ireland, whether that is to the Netherlands or to Bermuda?

Matt Brittin: I do not have a number on royalties—I do not think we have anything we would describe as royalties. The revenue earned by Ireland will have a bunch of costs against it, including the 3,000-plus people, the property, the data centres and so on, and then, yes, some costs associated with the international business as we have talked about earlier.

Q567 Stephen Barclay: So you do not pay any royalties from Ireland?

Matt Brittin: I don't know that I would describe it as royalties, but again, I think I promised to provide you with more of a breakdown on Ireland.

Q568 Stephen Barclay: Perhaps you could just clarify, because the SEC filings for Google say that the total amount of foreign income before tax was \$7,633 million. The foreign tax charge for the year, including deferred tax, was \$248 million, which is equivalent to 3.25%.

Matt Brittin: Of revenue.

Q569 Stephen Barclay: \$248 million, which is equivalent to a tax rate at 3.25%.

Matt Brittin: Of revenue.

Q570 Stephen Barclay: Yes.

Matt Brittin: Well, tax is paid on profits, obviously.

Q571 Stephen Barclay: No, on the income—income before tax.

Matt Brittin: I am sorry. I struggle to hear you.

Q572 Stephen Barclay: So the total amount of foreign income before tax was \$7,633 million and yet the tax charge for the year including deferred tax was 248 million, which is equivalent to 3.25%, and that is in your—Google's—SEC filings. I was just trying to establish how you got to that.

Matt Brittin: Well, in 2011 we paid \$1.5 billion of corporation tax in the US, which is an effective rate of—

Q573 Stephen Barclay: No, this is on foreign income, not what you paid in the US on your US income. This is about foreign income.

Matt Brittin: I do not have the figures to hand, but again I am very happy to answer any specific questions you have.

Q574 Chair: It is your bit of the world, Mr Brittin. That is the bit you are responsible for.

Matt Brittin: I am responsible for northern Europe, which is a part of the international, but not, by any means, all of the international.

Q575 Stephen Barclay: Sure—the money from which is ending up in Bermuda. What we are trying to establish is, in your SEC filings—you yourself said this is a US company—as I understand it there are SEC rules or there are IFS rules about passive income. So one of the ways round that is to check the box and say “This isn't money coming back into the US; it is going in to be parked, possibly, in Bermuda.” You are telling the US authorities that actually the foreign tax charge for the year is just \$248 million. The question

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in my mind is: to what extent in essence are you depriving the US taxpayer? Because you are saying to the US taxpayer, "Actually, there is only \$248 million of taxable income here," which works out at 3.25%. So the implication is that a lot of the profit is being stripped out somewhere.

What is unclear to me at the end of today's session is this: is it being stripped out; and, if so, where is that happening? Is it happening in Ireland, through royalty payments elsewhere, which was a discussion we had earlier around the 6% and 4.7% rates? Is it going into the Netherlands; or is it being parked in Bermuda? The implication of your SEC filings is that a very low tax rate in terms of the US is being paid on your foreign income. We have established today that you are not paying tax on the income from the UK. So it is very unclear where the tax is being paid in the chain.

Matt Brittin: We are paying tax on our UK limited business, as I have mentioned a number of times.

Q576 Stephen Barclay: Negligible.

Matt Brittin: We are paying corporation tax based on the activity that is carried out here.

Q577 Chair: Based on the activity you choose to file in Britain. It is the activity you choose to file. That is the great distinction.

Matt Brittin: But I think the distinction here between what I have been talking about and what we have been discussing earlier with consumer sales businesses is that the technology is US technology.

Q578 Stephen Barclay: It is the SEC filings that I would like you to refer your answer to.

Matt Brittin: I was just correcting, again, the fact that we pay corporation tax in the UK, as we are required to do. In the US—I haven't got the figures, but if you are quoting from the SEC filings of course they are correct—I am sure it is the case that we pay more tax on the US-earned revenues than we do on the revenues in the rest of the world; and I can answer the questions, as I promised to do, that you raised earlier on that.

What I would say is, as an international business that is a US-owned business, we make choices about where we locate and how we set up our structure, in order to ensure we can operate successfully and to minimise the costs and do the efficient things to run our business. That is what we are required to do by shareholders and by law, and that is what we do: play by the rules and manage our business efficiently.

Q579 Chair: Okay, let us go on to some general questions. Do you—all of you—accept that alongside your duties to your shareholders, which Mr Brittin has just alluded to, you have obligations to the societies in which you operate, and from which you derive huge benefits, and that those obligations include paying tax?

Q580 All witnesses: Yes.

Q581 Chair: And do you accept the principle that profits should be taxed in the countries in which they are made and where genuine economic activity is concerned?

Troy Alstead: Very much so.

Andrew Cecil: Yes.

Matt Brittin: Profits should be taxed in the countries where the economic activity takes place that drives those profits—so in our case where the innovation

takes place. Our business is made in California—that is the fact of the matter.

Q582 Chair: This is remarkable.

Matt Brittin: We are not making cups of coffee. We are making a search.

Q583 Chair: If you accept that—I think we have been through coffee that we know we drink in the UK, to books that I know I get in the UK, to Google ads that I know are just UK search engine-specific—why on earth do you manipulate your accounts so that you get away with not paying corporation tax, which is what this afternoon is about, in the UK? Mr Alstead?

Troy Alstead: Respectfully, I would disagree with that characterisation. Chair, we do not manipulate ever anything anywhere. We work very hard to be very honest.

Q584 Chair: Oh, Mr Alstead, you can't say that.

Troy Alstead: It is very true.

Q585 Chair: You can't say that you don't manipulate the royalty charge—in your case it is the royalty charge. It is manipulation of the charges for loans that you make the UK wholly owned subsidiaries take out, and the price of coffee. You charge 20% whatever the price is. That is manipulation. It takes money out of the UK that would otherwise be viewed as profit and would be taxed through corporation tax. It is manipulation.

Troy Alstead: Respectfully, those jurisdictions require us to report profit where the activity happens. We have no choice but to do that.

Q586 Chair: No, it isn't where the activity happens. You choose to charge 20%. You choose to take 20% for your Swiss coffee. You choose the 60% royalty—you actually told us it is what you could get away with and there was not a basis for it. You choose to charge above market rates for borrowing. You choose that.

Troy Alstead: No, I completely disagree with that characterisation, Chair, respectfully. That is not at all how we approach it. All of the rates that you referred to have been heavily scrutinised by valuation experts, by independent third parties who fully agree with those rates—that they are appropriate and fair—and by the taxing authorities all around the world. We do nothing—nothing—to avoid taxes.

Andrew Cecil: We set up our business across Europe for the benefit of our tens of millions of customers and sellers across Europe. We pay all applicable taxes in all jurisdictions.

Matt Brittin: We operate compliant with the tax law in the UK. We had a discussion this afternoon about Bermuda. Let me reiterate the fact that the tax we pay in the UK is nothing to do with anything outside Europe. What we do in the UK—we love the UK; it is a successful country for e-commerce. We think we have been part of that.

Q587 Chair: We think you should put a bit more money back in.

Matt Brittin: We follow the rules that HMRC lays out when they say we should be taxed on the activity where we generate our profits. For us, that is all of the engineering work that is done in California. I wish we had invented Google in Cambridge ideally, but we didn't; it is an American business and the engineering activity continues to be led from there.

Q588 Chair: Can I just get a feel of how many sets of accounts have yet to be agreed in your business, Mr Alstead?

Troy Alstead: In the UK?

Chair: In the UK.

Troy Alstead: The years 2010 forward are under review.

Q589 Chair: You've agreed everything before that?

Troy Alstead: Yes.

Q590 Chair: And Mr Cecil? How many sets of accounts have yet to be agreed?

Andrew Cecil: As I said, we are regularly audited.

Q591 Chair: How many sets of accounts have yet to be agreed with HMRC?

Andrew Cecil: I do not have that specific figure. I will come back to you with it.

Q592 Chair: How many set of accounts have yet to be agreed?

Matt Brittin: Our accounts for 2011 are with Companies House.

Q593 Chair: No, not Companies House. With HMRC, the tax bases.

Matt Brittin: They would be available to HMRC as well. The year is closed for 2011 and I don't think there are any outstanding issues, but if there are, we will let you know. HMRC has not told me that there are.

Q594 Ian Swales: Can I ask another general question? Do any of you have any discussions internally about issues such as consumer power and the value of your brand, and how that could be influenced by the ethical behaviour or perceptions of your company? How do you factor that into the sort of discussion we have had this afternoon?

Matt Brittin: Everybody who uses any Google service has a choice. All of our services are free to consumers, so we work extremely hard to try to ensure those services work well and that those consumers feel a level of trust in us. We talked earlier about the statement, "Don't be evil." For us, that means that when we give you websearch results we try to give you the best and most neutral results we can. That is how we operate. If consumers did not like what we were doing they would go elsewhere. There is plenty of choice. If you want to buy something you can go to Amazon. If you want a job you can go to Monster. If you want the news, you can go to the BBC. That is definitely at the forefront of our minds every day.

Q595 Ian Swales: Before the others answer, my question is not just about right now; it is about the trend that seems to be occurring—I am sure we have some representatives at the back of the room. People are now starting to say, "Don't deal with this company, because they don't behave ethically." That could be to do with paying taxes.

Matt Brittin: It could be. One great benefit of the internet is that it has brought an awful lot of transparency and an ability for consumers themselves to publish information and to be heard. That is a good thing. We very much support freedom of speech on the web. We want to hold ourselves to high standards. I hope I have tried to explain as transparently as possible this afternoon how we operate. I will happily answer any follow-up questions you have. Absolutely,

our business is completely built on trust of consumers. They won't come to us if they don't like the service.

Q596 Ian Swales: Can the other two quickly answer? The question is around consumer power and what your brand says, particularly in relation to ethics and taxpaying and so on.

Andrew Cecil: We are a company that is 100% focused on our customers. As I explained to the Committee, that is how we set up our business across Europe. We do listen to feedback from our customers.

Q597 Ian Swales: In your case, if I go to your website, why do you not make it clear that I am dealing with Luxembourg? Why do you have a misleading web address? Why does it look as though I am dealing with the UK when I log on to your website? That is not transparent.

Andrew Cecil: I disagree. I do not believe that it is misleading.

Q598 Ian Swales: It is absolutely misleading. You have been telling us all afternoon that we are dealing with a European company based in Luxembourg. Why does it look as though I am dealing with a UK company when I go to your website?

Andrew Cecil: I disagree. We make it very clear. You will see in all the communications that we make by e-mail and others that you are trading with a European company.

Ian Swales: I will go and look at the small print afterwards, but I bet it's very small print.

Q599 Stephen Barclay: Just building on Ian Swales's question, why did Amazon.com International transfer ownership of Amazon.co.uk to a company for one day, which then sold it on to Amazon EU Sarl? Could you explain that transaction for us?

Andrew Cecil: I will make a note of that and come back to the Committee.

Chair: I think somebody who can answer it will have to come back. I am just trying to look at today's thing. It does not say anything about my dealing with—all over this e-mail I received from you today, it says Amazon.co.uk. I can see it once, twice. It says "see Amazon.co.uk" and "Your Amazon.co.uk" and "Dear Amazon.co.uk customer, Shop now."

Q600 Ian Swales: See if you can find the word "Luxembourg" anywhere.

Anyway, there is obviously—justified or otherwise—a fair amount of media interest in Starbucks' activity, which is perhaps a good example of why I am asking the question, because surely, from your own corporate point of view, you have to think about the risks you run in how you structure your organisation and the taxes that you pay in terms of what your customers think about you as a result.

Troy Alstead: Yes, it matters critically what our customers think about us. We discuss it frequently and all the time. It is one of the key pillars in the company. We have huge commitments to all the communities that we operate in, including the UK. We have committed to creating 5,000 new jobs here and 1,000 apprenticeship positions—investing in the community. We are also committed to paying corporation tax as we improve the profitability of our business.

Q601 Ian Swales: You are not the most opaque this afternoon by a long way, but how do you feel about transparency? How clear should companies such as

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yours be in explaining what they actually do worldwide, where they operate, and what taxes they pay in the different countries where they operate? It should not just be for the sake of transparency, but to convince your customers that this is the kind of company that they want to do business with.

Troy Alstead: We believe very strongly in transparency—with the Committee, with tax authorities around the world and with consumers—recognising that one of the challenges that we often face is that the global tax structure is very complex. It is very difficult to explain it, and that is without having anything to do with avoidance. It is just a difficult challenge.

Q602 Ian Swales: But that is partly because you make it so. I do have experience in this area so I am not being entirely simplistic, but if you run a business in this country, that country, and another country, it is clear what your profit is. If you transfer money between them, you can make it clear what the basis is. It does not need to be that complicated.

Troy Alstead: The reason it is difficult to explain at times is that if we did not buy those services for the UK business, we would have to build an R and D centre in the UK.

Ian Swales: Just be transparent. You buy the services. Just tell people what you buy and what it costs. That is transparency. I am not saying that everything has to be in one country, but there should be transparency in why you do certain things. That is probably enough from me, but it is one of the themes that has come out today.

Q603 Jackie Doyle-Price: I think the difficulty, Mr Alstead, is that the British consumer feels misled. We are where we are and you are dealing with the international tax situation as you, as a company, see fit, having branded Starbucks as something that has a very high standard of ethics, but the British consumer is left thinking, “This is a bit smelly.”

Troy Alstead: I appreciate that. That is very unfortunate and we feel terrible about it. We honestly feel as though we have not intended to mislead anybody. We are trying to be very transparent. I appreciate that the media attention has made it look that way, so we need to do a better job of finding a way to communicate. I assure you that our intent is to operate at the highest ethical standards.

Q604 Fiona Mactaggart: Mr Alstead, you said earlier to the Committee that you don’t have any Cayman tax haven. I am looking at a listing of subsidiaries of Starbucks corporation under the SEC—the American listing rules—of 2 October 2011, which lists a company called President Coffee (Cayman) Holdings Ltd. I would be very grateful if you could tell us now, or possibly later, what that company does.

Troy Alstead: I can tell you very clearly now. President Group, which is what that structure is named after, is a Taiwanese company. They are also a joint venture partner with us in mainland China. Mainland China has not allowed, as you can imagine, Taiwanese companies to own businesses directly, but they do allow them to own them indirectly—that can be fully validated, by the way. So our Taiwanese partner established a joint venture in the Cayman Islands,

which then becomes the owner of their investment on mainland China. There are zero tax implications, I assure you—zero—but it allows our Taiwanese partner to be a partner with us in mainland China.

Q605 Meg Hillier: I want to focus on Google and Amazon, and the challenge for the tax authorities in the UK and, in fact, around the world about pinning down tax from companies that are internet-based. It is a big challenge. We have raised concerns about how some of you operate. Do you think that the OECD definition of what a branch is should be updated for the internet world, first of all?

Matt Brittin: I don’t have the definition in front of me. I would be very happy if you want to send it and we can comment back. I recognise the challenge of a very fast developing environment with the internet. One of the things that I spend some time doing is trying to help people understand and think through those issues. We are proud of how we operate. We try to operate transparently. We definitely operate in line with the law in every country in which we operate.

Andrew Cecil: We don’t have a specific view, but we do apply the OECD principles and we would be happy—I agree with Matt here: it is a very fast moving world. I understand in fact that the OECD guidelines are currently being consulted upon.

Q606 Meg Hillier: That brings me to the other question that leads into, which is do you think that the tax affairs that you have the option of operating under are too complex, or is it that you make them complex, by having companies in Bermuda, for example?

Matt Brittin: When I first arrived at Google, I was aware of the issues of multinationals generally operating and I wanted to understand how we operated and the ways in which we complied with tax law. I found that it is a complicated system. I am not a tax expert—my job is to run the business—but I also found that we comply with the law and what we do is in common with many other companies that are intellectual property driven. The challenge for Governments like the UK Government is to think about what the right set of policies is to encourage competition, innovation and investment in your country when every country in the world can set the tax rates and regimes that they want. It is a complicated area. I am pleased with and proud of how we operate in that area. Any international company has to make those kinds of choices on how to operate, but it is complicated.

Q607 Meg Hillier: Do you know how much you spend on tax lawyers?

Matt Brittin: I don’t know.

Meg Hillier: Could you perhaps write to us?

Q608 Chair: Who advises you? I was going to ask the same question. You run the company. Who advises you on tax?

Matt Brittin: We have a small internal team on finance. Ultimately our chief financial officer in Google Incorporated in California is responsible for our tax policies. We have a small team in Dublin.

Q609 Meg Hillier: You buy in as well, presumably?

Matt Brittin: I am sure they go externally for advice, as you would expect.

Q610 Meg Hillier: It would be helpful if we could write to you, or if you could come back to us.

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Matt Brittin: Absolutely.

Q611 Chair: This is the very final question. The Prime Minister has said he is not happy in answer to a question from me in the House. The Business Secretary has branded you all a disgrace. The Chancellor has said that present arrangements allow you “to pay less tax” than you would otherwise owe. Can I have your response to those views expressed by the leaders in the UK?

Troy Alstead: Very disappointing, Chair. I understand it, given the confusion. I hoped that today would allow us to clear up some of the confusion. If not, we will keep working at providing the Committee with additional information and communicating with our customers more clearly. We sincerely believe that we are doing everything to an ethical standard—not just the legal standard, but exactly what we should be doing. We will continue to do our best to communicate that both here and with our customers.

Q612 Chair: I think, Mr Cecil, you probably cannot answer the question, so we might skip you.

Andrew Cecil: We will continue to operate our business on behalf of our customers and sellers across Europe. For their benefit, we will look to see how we can reduce prices for them and drive selection. If

Governments decide to change these rules, we will see how we continue to comply with all corporate laws.

Q613 Chair: We hope to have a session in a week or two when somebody from Amazon can answer questions. And you finally, Mr Brittin?

Matt Brittin: I presume that those were general comments made about a range of companies rather than us specifically.

Chair: No. You were named. Certainly in the question that I asked the Prime Minister, you were named.

Matt Brittin: We comply with the law in the UK. It would be very hard for us to pay more tax here based on the way we are required to structure by the system. Tax is not a matter of personal choice, but a matter of following the law and the rules, which is what we do. It is complicated internationally, but we follow the law in every country in which we operate. The fundamental issue for us is that our economic activity, which generates the algorithms that make a lot of products work, comes from engineering that is all coming from California. That is why we pay tax where the profits are generated, which is how the tax system operates.

Chair: Thank you very much for having a dialogue with us this afternoon.

Written evidence from HM Revenue and Customs

1. **Q30 Chair:** *You have 770 large businesses and the figure that we had from you last year—I accept that it was a potential figure and not the nth number—was £25 billion outstanding. That was the figure that the NAO had in its Report last year. How many of those 770 large businesses had a parent company outside the UK?*

The number of companies managed by the Large Business Service has increased and it currently has 783 customers, of which 371 have non-UK parents.

2. **Q34 Chair:** *About half, okay. You treat them all fairly, but is it also true that there has not been one litigation against a large business since 2004? Am I wrong in that? I hope that you are going to tell me that I am.*

The department has taken litigation action against a number of large businesses and refers the Committee to the written evidence that was provided on 13 July, 2012 (Q.162–168) following the PAC Hearing on 27 June 2012: Tax Disputes:

“There are currently just over 1,000 instances of litigation involving taxpayers defined by HMRC as “large businesses” (turnover exceeding £30 million or more than 250 employees).

We estimate the number of large corporates involved in litigation to be 600 (a number of these are involved in more than one of the instances of litigation referred to above).

In the very largest business cases (the 770 dealt with by the Large Business Service), our systems also show approximately 750 issues under enquiry where the issue is similar to one already in litigation in another case. In such cases businesses often do not enter into litigation but resolve the enquiry by agreement following a decision by the Courts on the point of principle in a similar case.

HMRC currently wins about two-thirds of its disputes with large businesses at Tribunal and in the five years to 2010–11 roughly a quarter of Large Business Service compliance yield (£6 billion) came from litigation.

In his oral evidence to the Committee on 27 June 2012, Jim Harra said that there are currently just over 4,000 live litigation cases in HMRC’s solicitor’s office. We have checked this figure and in fact there are 8,154 live litigation items of litigation. Of these items just over 1,000 involve taxpayers defined as “large businesses”.

3. Q46 **Austin Mitchell:** *Can you tell us how many of the big corporations are handling their tax affairs through offshore tax havens?*

HMRC's Large Business Service deals with the tax affairs of the 783 largest businesses in the UK.

- Most of these businesses are multinationals with complex international structures, including operations in both countries with lower tax rates than the UK and countries with higher rates.
- As part of HMRC's business risk review process, our Large Business Customer Relationship managers obtain a detailed understanding of each group's corporate structure, including their presence in lower tax jurisdictions. This information informs the tax risk assessment and the selection of areas for investigation.
- HMRC applies corporation tax rules, such as the transfer pricing rules and the controlled foreign company rules, to ensure that the correct profits are charged to corporation tax in the UK.
- VAT operates differently from corporation tax, and is normally charged in the country where the customer is located. Until 2015, when the rules will change, a significant exception to this general rule is the supply of electronic services. HMRC has robustly challenged suppliers of electronic services to UK customers who claim to have re-organised their corporate structures to take advantage of lower VAT rates in other EU countries. See HM Revenue & Customs: Spotlight I VAT: Relocation of telecommunication service providers, Internet service providers and broadcasters (9 February 2011).
- In the year ended 31 March 2012, HMRC's Large Business Service recovered £5 billion additional revenues from the 783 large businesses it deals with. Approximately 1/3 of this came from the investigation of international tax risks, such as transfer pricing and controlled foreign companies. HMRC recovered £4.7 billion additional revenues from transfer pricing enquiries in the five years to 31 March 2012

4. Q105 **Chair:** *Okay. I get that, but can you tell us, or will you write to us, about how many cases you do not pursue through debt collection agencies, but you may pursue through the courts? You do not know how many cases you have against the top businesses at the moment, do you? You talked about some of your successes, but you have not got a list.*

See response to 2 above.

5. Q131 **Mr Bacon:** *Sorry, that was not my question. My question is about individual records. It says 1.5 million individual records; my question is how many individual records you have got now, if it was 1.5 million at the end of May?*

At the end of Stage 2 the number of employee records at that time was around 2 million (1,977,426) reported by 1882 PAYE schemes. Stage 3 of the pilot started on 6 November and at the end of day 1 the total individual records had increased to 2,128,426 employments, being reported by a total of 6,827 PAYE schemes.

6. Q171 **Mr Bacon:** *What I would like to know is this. Perhaps you do not have this answer, but lots of work goes on in the DWP—and, I imagine, also in HMRC—that is based on estimates, worked examples and extrapolation. Do you have any figure for the number of people who simply do not claim tax credits at all, because they want to have nothing to do with it, because they are fearful that they will end up in a situation where they are overpaid, even though they are entitled?*

The latest published take-up statistics for 2009–10, which are available on the HMRC website, show that around 2.7 million households (1.4 million families with children and 1.3 million households without children) were eligible for, but did not claim, tax credits.

The 2010–11 estimates will be published on 12 December 2012.

7. Q175 **Mr Jackson:** *Can I ask you about the specific issue of child tax credits? My constituents get slightly concerned when they hear about the number of child tax credits that are going to EU citizens whose children do not reside in the UK and are likely never to reside in the UK. You will say that is a relatively small amount.*

What concerns me slightly is that until recently you have not collected—or rather the Treasury has not been willing to divulge even that it attempts to estimate the number. I just wonder whether you collect data on that. Would you know how many, what countries and on what basis and, more importantly, what is the practicality of checking the veracity of those claims?

The Committee's attention is drawn to the written answers given by the Exchequer Secretary to the Treasury to the Hon. Member for Dover on 25 October 2012 (Official Report Column 1022W).

“Out of a total of approximately 5.2 million families currently receiving the child tax credit for almost 9.3 million children, at 30 September 2012 there were 3,447 ongoing awards of the child tax credit under EC Regulation 883/2004, in respect of 5,962 children living in another member state. This equates to around 0.06% of all child tax credit awards.

Information about the value of child tax credit awarded by the UK under EC Regulation 883/2004 is available only at disproportionate costs. This is because under the priority rules in that regulation not all awards of UK family benefits are made at full UK rates.”

In addition to the risk-based checks applied to all claims for tax credits, HMRC undertakes additional checks where a claim is made to which EC Regulation 883/2004 may apply. In co-operation with the relevant authorities in the Member State where the family resides, we check to confirm the composition of that family, whether a migrant worker’s spouse is working in that other Member State and whether that other State’s family benefits are in payment. HMRC does not make payments of child tax credit (or child benefit) until the authorities in the other Member State have provided the necessary information. These are well-established procedures which apply across the EEA, involving the use of standard forms by the authorities of all Member States. There are EU plans for electronic exchange of information between all Member States (Electronic Exchange of Social Security Information programme) which, once implemented, will make these checks easier and faster.

8. Q179 **Chair:** *This one is on PAYE—the reconciliation on PAYE. Your latest figure is £53.7 million for the tax that has been lost through various things—money coming in too late and getting money out of people late. You are also raising the level at which you pursue people. What is the final total? If you have finished all these reconciliations, what is the final total of moneys lost to the Exchequer because of the mess in which this reconciliation occurred over time?*

In the previous report on HMRC Accounts, we advised that we remitted 28,000 claims amounting to £41 million in respect of Extra Statutory Concession Article 19 (ESC A19) for the period September 2010 to June 2011. For 2011–12 a further £12.7 million was remitted during the period from July 2011 to March 2012. Therefore, latest figures of £53.7 million remitted refer to the total amount of revenue foregone from September 2010 to March 2013. This covers the whole period of processing Pay As You Earn (PAYE) since the introduction of the new PAYE computer system, called the National Insurance and PAYE System (NPS).

£12.7 million is a considerable reduction on ESC A19 remittances compared to 2010–11 and this trend will continue because we are more up to date with PAYE processing.

In respect of the question about total monies lost to the Exchequer due to the activity necessary to introduce and stabilise NPS and bring PAYE up to date, the department has not changed its previously shared estimates and continues to estimate the revenues foregone for the application of the £300 PAYE tolerance for years 2008–09 and 2009–10 as £160 million, and a further £166 million for the extension of the £300 tolerance applied to 2007–08 underpayments. In addition, as previously stated, £100 million was foregone from the diversion of resources to recovery work from 2006–07 underpayment cases.

Total Income Tax remissions were £756 million for 2011–12 but this figure also includes all underpayments under the tolerance threshold worked during 2011–12 across all PAYE work (both current and legacy) and across all tax years.

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Written evidence from Starbucks

Starbucks Coffee Company respects and complies with tax laws and accounting rules in each of the 61 countries where we do business, including the United Kingdom—a market that we remain committed to for the long term. As a company, we have always believed that to be successful we must do our best to strike a balance between profitability and social responsibility, and we will continue to strive to meet our own high ethical standards for how we care for our people, source our coffee, serve communities and operate in the countries where we do business.

STARBUCKS IN THE UK

1. Starbucks entered the UK market in 1998 with the acquisition of The Seattle Coffee Company which then operated 60 stores in the UK. We now operate more than 700 stores and through our licensees provide the rights to operate a further 200 stores in the UK and Ireland; as such we employ nearly 8,500 partners (employees) here. In December of last year we announced that Starbucks would be creating 5,000 new jobs over the next five years, as we directly and in conjunction with our licensees open 300 new stores up and down the country.

2. Starbucks is proud to be making a net positive contribution to the UK. Our presence in the UK has created benefit to the Exchequer. For example, over the last three years we have contributed more than £160 million to the Exchequer in various taxes, including National Insurance contributions, Stamp Duty, Insurance Premium Tax, VAT and business rates.

3. However, Starbucks economic impact in the UK spans far beyond our stores and partners. We have spent hundreds of millions of pounds with local suppliers on milk, cakes and sandwiches, and on store design and renovations. In fact, when you consider the indirect employment created by Starbucks investments in the UK,

the company's extended economic impact directly to the UK economy is even more significant and exceeds £80 million annually.

4. In addition to the thousands of new jobs which will be created through our operations over the next few years, we recently committed to creating 1,000 apprenticeships to give young people the opportunity for great careers in retail. This program complements our partnership with UK Youth, a nationwide youth charity, to provide seed funding for young people to undertake community improvement projects in their local communities. We also have an ongoing partnership with the Prince's Trust to provide work experience and life skills to young people Not in Education Employment or Training (NEET).

OUR EMEA AND UK BUSINESS STRUCTURES

5. Our EMEA (Europe, Middle East & Africa) business is headquartered in Amsterdam which provides a central location and a skilled multi-language labour force. It manages operations in 33 countries. Also in Amsterdam is our roasting facility which roasts all coffee beans used in Europe before distributing them to the various markets—the primary reason we selected Amsterdam for our EMEA headquarters.

6. In Lausanne, Switzerland, a global hub for commodity trading, we operate a global coffee buying business. Coffee beans are currently the second most traded commodity in the world and we achieve major economies of scale from centralising this activity in one place. It is also important to note that 75% of the world's coffee is traded through Switzerland and Starbucks represents less than 5% of the annual coffee trade.

7. We rightly pay a premium for the beans in all our espresso beverages because they are 100% Fairtrade certified. Coffee is one of our major cost components and while we could acquire cheaper coffee, our belief has always been that we should source the highest quality, ethically-sourced coffee. No other major coffee chain in the UK purchases 100% Fairtrade certified espresso.

8. Starbucks in the UK is registered as Starbucks Coffee Company UK Ltd. Our UK headquarters is in Chiswick, West London. Our UK operation is responsible for directly running all stores and product marketing in the UK as well as managing our third party licensee relationships. Other significant business activities such as product development, brand development and trademark protection are carried out either at EMEA level in Amsterdam, where we employ 220 partners in our offices and roasting plant or at global level in Seattle.

9. Finally, it is important to note that Starbucks overall corporate tax rate is nearly 33% for 2012. This compares to a median effective rate of 18.5% for large multinational US companies.

A SUMMARY OF OUR TAX AFFAIRS IN THE UK

10. Over the last 14 years we have paid £8.6 million of corporation tax in the UK. Corporation tax is a tax on profits and the simple fact is that it has been difficult for us to make a profit in the UK under any measure. Under the rules we are required to follow when reporting our US results, which exclude royalty payments and interest expense, our most profitable year (2007) in the UK had an operating margin of only 6%. It has been stated several times in the press recently that our UK operating margin using our US reporting method has reached 15%. This is categorically incorrect and we have never stated publicly or in our internal records that our UK profit margin has been near 15%.

11. Our lack of profitability in the UK is a source of concern to us as a business. There are a number of reasons behind this. One significant factor is the cost of leasing property in the UK. In the US, property costs amount to around 10% of sales revenue, whereas in the UK they represent around 25% of sales revenues. Nevertheless, our business in the UK is improving and we are restructuring our property portfolio significantly to counteract this. Another factor is that this is a very competitive market to sell coffee and we have to work very hard to attract and retain customers and as noted above, we are committed to providing only ethically sourced coffee. We are optimistic we will become more profitable in the coming years and with 13 consecutive quarters of sales revenue growth on a like-for-like basis behind us, we are moving in the right direction.

12. A large degree of scrutiny has attached itself to the "royalty payment" of 6% we make to our EMEA headquarters in Amsterdam. Charging a royalty payment for the right to use a global brand and for services provided is standard business practice for multinationals. When marketing fees are included, our royalty rate compares quite favourably to other multi-national licensors. As noted above, the royalty also reflects the services provided to Starbucks UK and includes product development, marketing, brand development and trademark enforcement and protection as well as IT and accounting functions in the regional and global headquarters. Were these services not provided to Starbucks UK internally we would have to fund them locally, at much greater cost which would further impair Starbucks UK's ability to be profitable.

13. It has been discussed that Starbucks financial reporting in the US has suggested a different level of profitability in the UK compared to that declared to HMRC by the UK business. This is simply and entirely due the different requirements that American and UK tax authorities place upon the way we file our accounts. Specifically, US accounting rules (US GAAP) require us to exclude intra-company royalty payments and loans interest for tax filing purposes whereas UK rules require us to include them. Starbucks UK, as a subsidiary of a US multi-national company, is obliged to follow US GAAP principles.

14. We would like to reiterate for consideration that corporation tax is only one of a multitude of taxes businesses pay. Taking into account business rates, VAT, employer national insurance contributions, Stamp Duty and other business taxes, we estimate our overall contribution to the Exchequer amounts to be over £160 million over the last three years. We also employ around 8,500 people and, as noted above, directly and indirectly in our supply chain activities and through our licensees are hoping to create thousands of jobs in the UK. Our point is that Starbucks makes a net positive contribution to the UK and we are proud to do so.

HOW WE WORK WITH HMRC

15. We respect the difficult task HMRC faces in administering taxes across many tax jurisdictions. This administration requires working with other tax jurisdictions to determine the amount of tax revenue each jurisdiction is entitled to, based upon activities carried on in each jurisdiction. Each jurisdiction is competing for tax revenue dollars as well as competing to attract business to their jurisdiction. Our relationship with HMRC is nothing other than professional. We have always been willing to engage and, in our belief, have been nothing other than cooperative and respectful. We consider this an appropriate relationship between a company and its tax authority and it reflects how we work with equivalent bodies in countries around the world.

16. HMRC has completed an extensive audit of our tax years FY 2003 to FY 2008. This audit resulted in a reduction in our tax deduction for the royalty payments from 6% to 4.7%. We are currently engaged in negotiations with HMRC to reach an agreement on the appropriate tax deduction for our royalties from FY 2010 to FY 2016.

STARBUCKS FUTURE IN THE UK

17. Over recent years we have been restructuring our business in the UK to position it for further growth. In particular, this has involved managing our property costs downwards, deploying new format stores such as drive-thru which trade very effectively, and diversifying into at-home coffee machines, franchising and vending. There can be no doubt that we are trying to grow.

18. The overall strategy for the UK is continuing investment which creates jobs, expands the business and—ultimately—will see us become a profitable operation in the coming years. We announced in December that we are aiming directly and through our licensees to open 300 stores and create net 5,000 jobs in the UK in the next five years.

19. As we return to profitability our tax responsibilities will change and we anticipate paying greater amounts of corporation tax in the UK in the future and at the same time our overall tax contribution will continue to escalate.

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Supplementary written evidence form Starbucks

Further to the Public Accounts Committee hearing of 12 November, please find below additional information requested by the Committee.

Q214–229: ROYALTIES:

Starbucks UK and other Starbucks operating units in our Europe Middle East and Africa (EMEA) Region pay a 6% royalty to this region's Amsterdam headquarters. The 6% payment is standard business practice for multinationals in the food and beverage sector and reflects a payment for services provided by Starbucks Coffee Company and Starbucks EMEA headquarters. It is a market-based payment and we have over 20 unrelated third party licensees that have also agreed to pay this royalty at a consistent rate across the world. Many of these third party licensees are large, sophisticated companies that know very well how to value the brand and services they receive from Starbucks.

The value Starbucks UK receives for the 6% royalty includes:

- Rights to the Starbucks brand and trademark, one of the top 100 brands in the world and in the UK. Starbucks registers this trademark in every country it operates and actively protects this trademark, spending millions of dollars a year building and protecting our brand and other assets.
- The highest quality and ethically sourced Arabica coffee. The way we roast coffee is proprietary to Starbucks. Licensees have access to more than 20 core coffee blends, seasonal products and rare single origin Starbucks Reserve coffees.
- Expertise to deliver excellent customer service through store operations, in-depth study of front and back of house operations, quality control, management, merchandising, budgeting, and expense control; including comprehensive training programmes and detailed manuals covering every aspect of retail operations.
- Use of the Starbucks proprietary business model, including numerous standard and promotional beverages and other offerings, including an integrated customer loyalty programme and mobile payment platform.

- Store design concepts which provide customers with a comfortable and accessible environment which address the needs of the local market.

Our royalty rate is subject to the scrutiny of tax jurisdictions across the world. Our consistent royalty rate with over 20 unrelated third parties around the globe is the best evidence that the “transfer pricing” of our 6% royalty rate is arm’s length—a market rate royalty. When marketing fees are included, our royalty rate also compares favourably to other multinational licensors.

We have not created an analysis of the breakdown of the underpinnings of our royalty for either commercial or internal purposes. Nor have we needed to do so. For example, in negotiations of our royalty rate with unrelated third parties, we present a combined number of all the value received for the royalty. In these negotiations, we do not attempt to breakdown the underpinnings of the value of the royalty, as this is not typically requested by our commercial licensees. However, as an indication of the scale of some of these activities, we spend approximately \$500 million per year for costs related to marketing, brand and product development, store design, and research and development.

Even if it is assumed our UK business paid no royalty during the last 10 years, given the poor performance of our UK business Starbucks UK would have only paid 2 million GBP of total additional corporate income tax during this period.

Q239: COFFEE COSTS:

The price that Starbucks UK pays for coffee is consistent with the price we charge to over 20 unrelated third party licensees. Many of these third party operators are large, sophisticated companies that know very well how to value the Starbucks-branded coffee and they purchase approximately 25 million pounds of coffee at rates similar to those paid by our UK business. The fact that Starbucks has centralised its roasting for our EMEA region in Amsterdam does not impact Starbucks UK’s corporate income tax results. For example, if Starbucks UK purchased coffee from Starbucks roasting facilities located in the U.S, the coffee price would be consistent and Starbucks UK’s corporate income tax results would be the same.

In fiscal year 2011, we paid an average of \$2.38 per pound for green coffee. We rightly pay a premium for the beans used in all our UK espresso beverages because they are 100% Fair Trade Certified. Coffee is one of our major cost components and, while we could acquire cheaper coffee, our belief has always been that we should source the highest quality, ethically-sourced coffee. We believe that by establishing direct relationships with coffee producers and by establishing quality standards we can help to ensure the sustainability and future supply of high-quality coffees. Our comprehensive approach to ethical sourcing—including farmer support centres, farmer loans and forest carbon programmes (through which farmers are incentivised to keep forests)—promote best practices in coffee production.

Q246: THE NETHERLANDS:

We pay both Dutch and US taxes on the royalties received in our Amsterdam structure. The transfer pricing of transactions within the structure are arm’s length and in accordance with transfer pricing guidelines set by the Organization for Economic Cooperation & Development (OECD). The overall effective tax rate we have paid on the royalties received by our Amsterdam regional structure has averaged 16% over the past five years.

Q276: SWITZERLAND:

The total income tax liability for FY2011 for our coffee procurement company in Switzerland was 11.6 million CHF.

Q282: RESEARCH & DEVELOPMENT:

Our research and development costs relate primarily to innovation in our products and equipment. Examples of innovations include our Frappuccino® blended beverages, Starbucks Refresha™ beverages, Starbucks VIA® Ready Brew and Verismo® System by Starbucks in-home coffee and espresso machines. Any information provided relating to our research and development costs do not include any intercompany profits. The costs are actual costs incurred by Starbucks.

Q284–286: CONFIDENTIALITY OF THE NETHERLANDS AGREEMENT:

As with all tax authorities around the world, there is a mutual understanding of confidentiality relating to information shared with and received from the Dutch tax authorities in our confidential but arm’s length negotiations with them. While we do not have a formal written confidentiality agreement with the Dutch tax authorities, we believe this mutual understanding is an important underpinning of our professional relationship with the Dutch tax authorities as it is with all tax authorities we work with.

Q318: THE NETHERLAND TAX PAID AND CONFIDENTIALITY AGREEMENT:

The amount of tax we paid to the Netherlands government is publicly disclosed in the Annual Accounts (financial statements) filed with the Dutch government each year. In 2011 we paid 715,876 Euros in tax to The

Netherlands. Please see the response to the question above regarding confidentiality with the Dutch tax authorities. HMRC has established channels with the Dutch tax authorities through which it can request additional information.

SUMMARY

In summary, we are committed to improving our business and becoming profitable, and in turn, increasing payment of UK taxes on these profits. As for payment and taxation of royalties for the services that are provided by our EMEA headquarters and US business to our markets, including the UK, taxation occurs primarily under the laws where business activities that generate the royalties occur. This global principle of taxation for companies operating in several markets is reflected in how Starbucks pays taxes.

We are committed to working with local tax authorities to determine the amount of tax revenue each jurisdiction is entitled to, based upon the nature of activities carried on in each market. While we do avail ourselves of the benefits of the tax laws in each country in which we do business, unlike many companies and individuals, Starbucks does not use island offshore tax havens which welcome shell companies usually run by one person with multiple entities under his or her control, and that traditionally have a tax rate of zero. Such tax havens are drastically different from Starbucks situation. We have centrally located Starbucks 8,719 square-metre EMEA regional headquarters, distribution center and coffee roasting plant in the Netherlands, where we employ approximately 220 multi-language partners and distribute approximately 15 million pounds of coffee to the 33 countries in which we operate across the region.

I hope this information is helpful to the Committee.

20 November 2012

Written evidence from Amazon EU SarL

Thank you for giving me the opportunity to appear before your Committee yesterday. I would like to provide the additional details you and the Committee requested about Amazon's EU structure and UK sales.

Amazon's European corporate structure is as follows:

- The rights to intellectual property used to operate Amazon's EU websites are held by Amazon Europe Holding Technologies SCS, a Luxembourg company. Amazon Europe Holding Technologies SCS is owned by Amazon.com Int'l Sales, Inc., Amazon.com, Inc., and Amazon Europe Holding, Inc., all of which are U.S. companies. This is how EU entities pay for the use of Amazon's technology and intellectual property, which is primarily developed in the U.S.
- Amazon's EU ecommerce retail businesses on all of our EU websites, including on www.amazon.co.uk, are operated by Amazon EU SarL, a Luxembourg company owned by Amazon Europe Holding Technologies SCS. Amazon EU SarL owns the inventory, earns the profits associated with the selling these products to end customers and bears the risk of any loss. From Luxembourg, Amazon EU SarL processes and settles payments from its European customers.
- Amazon's EU third party seller (*ie*, marketplace) business, which supports sellers that sell on www.amazon.co.uk, is operated by Amazon Services Europe SarL, a Luxembourg company owned by Amazon EU SarL. Our marketplace service allows small businesses and sellers to make their goods available through our Amazon's EU websites. In addition, these businesses and sellers can choose to send us their inventory in one country, which we store at our fulfilment centres, list on all our websites across Europe, and pick, pack and deliver anywhere in Europe. From Luxembourg, Amazon Services Europe SarL processes and settles payments from its European customers.
- Amazon's EU digital business (in which MP3s and eBooks are sold) is operated by Amazon Media EU SarL and is owned by Amazon EU SarL. Amazon Media EU SarL earns the profits associated with the selling of digital products to end customers and bears the risk of any losses. From Luxembourg, Amazon Media EU SarL processes and settles payments from its European customers.
- Fulfilment and customer service centres located in the UK are operated by Amazon.co.uk Ltd, a UK company. Amazon.co.uk Ltd earns a margin on its operating costs for providing services performed in the UK to group companies, primarily to Amazon EU SarL. The services provided include fulfilment and logistics services; customer support services; accountancy, tax, legal, human resources, localisation and similar back office services; merchandising and marketing support services; and purchasing assistance.

Although we have not publicly disclosed net sales generated from specific websites targeting EU countries or elsewhere, in response to the Committee's request, we would like to share with you on a confidential basis net sales generated from the amazon.co.uk website over the past three years. These sales are set forth in the table, below, along with the amount of VAT collected by Amazon EU SarL on behalf of the UK government.

<i>(in millions)</i>	2009	2010	2011
Net Sales: www.amazon.co.uk	£1,865	£2,360	£2,910
UK VAT Collected: Amazon EU Sarl	£172	£262	£416

Andrew Cecil

Director, EU Public Policy

13 November 2012

Supplementary written evidence from Amazon EU SarL

Thank you for the questions we received on Tuesday from the Committee of Public Accounts. I write to provide answers to those questions. For completeness, I enclose as an Exhibit a copy of my letter [Ev 56] to you dated 13 November which addressed a subset of these questions.

The table below provides 2011 sales originating in each European country, excluding countries from which sales did not exceed \$10 million. Sales from these other European countries, relating principally to the Nordic operations of our LOVEFiLM subsidiary, have been aggregated with our international businesses into "Other International."

The following sales amounts are not publically available at this level of detail, are unaudited, and are being provided solely for the purpose of responding to the Committee's questions. In our public company filings with the U.S. Securities and Exchange Commission, we disclose sales, operating expenses, operating income and information for our two business segments, "North America" and "International." The financial information included in this letter is derived from those data except for intercompany expenses.

Given the non-public nature of this information, we respectfully request confidential treatment.

Net Sales Twelve Months Ended December 31, 2011

<i>(in millions)</i>	<i>Currency</i>	<i>Local Currency</i>	<i>USD</i>
Germany	EUR	5,232	7,230
UK	GB	3,351	5,348
France	EUR	889	1,225
Italy	EUR	154	212
Spain	EUR	79	107
Other International			7,250
Total Net Sales International Segment			21,372
Total Net Sales North America Segment			26,705
Total Net Sales Worldwide			48,077

As shown in the table above, our sales from the UK for 2011 were £3,351 million, which consists of sales of £2,910 million related to orders on the amazon.co.uk website (as provided in our previous letter) and approximately £441 million in revenue from subsidiaries such as LOVEFiLM and from other business activity outside of the amazon.co.uk website.

Profits before income tax on our UK sales of £3,351 million were £74 million for 2011. Costs associated with these sales include cost of sales of £2,690 million; operating expenses of £417 million; intercompany charges of £151 million primarily for the use of intellectual property licensed from Amazon Europe Holding Technologies S.C.S.; £12 million of stock based compensation for the UK group of companies; and £7 million of other expenses.

As a point of reference, below is our International segment and worldwide consolidated statement of operations information (the amounts below exclude the impact of intercompany transactions):

<i>(in millions)</i>	<i>Twelve Months Ended December</i>		<i>Nine Months Ended September</i>
	<i>International Segment</i>	<i>Worldwide Consolidated</i>	<i>Worldwide Consolidated</i>
	<i>31, 2011</i>		<i>30, 2012</i>
Statement of Operations:			
Net Sales	\$ 21,372	\$ 48,077	\$ 39,825
Segment operating expenses	(20,732)	(46,504)	(38,836)
Segment operating income	640	1,573	989
Segment operating margin	3.0%	3.3%	2.5%
Stock based compensation		(557)	(597)
Other operating expense		(154)	(121)
Income from operations		862	271
Operating margin		1.8%	0.7%

In 2006, as part of the establishment of our European headquarters in Luxembourg, we transferred ownership of a group of companies, including Amazon.co.uk Ltd, from our U.S. subsidiary Amazon.com Int'l, Inc. to Amazon Europe Holding Technologies S.C.S., and then to Amazon EU Sarl. Part of this process was to register the shares of Amazon EU Sarl with the Luxembourg authorities, which took one day to complete. Our Luxembourg entities do not have any preferred equity securities outstanding and have never issued preferred equity securities.

As described in more detail in our previous letter to your Committee, attached, Amazon.co.uk Ltd, is a UK company that provides fulfilment and logistics services; customer support services; accountancy, tax, legal, human resources, and localisation services; merchandising and marketing support services; and purchasing services. Amazon.co.uk Ltd is compensated for these services by Amazon EU Sarl; therefore it is not a "branch" or "place of business" of Amazon EU Sarl.

Statements of account are prepared for entities throughout Europe, and when required, audited, based on the requirements applicable in each country and include the impact of intercompany activity. These statements are prepared on a basis consistent with local accounting standards and other regulatory requirements. I am enclosing as Exhibits [not printed] the requested 2011 statements of account for Amazon.co.uk Ltd, Amazon EU Sarl, and Amazon Europe Holding Technologies S.C.S.

Andrew Cecil
Director, EU Public Policy

16 November 2012

Written evidence from Google

1. *Could you provide information about how your shareholders benefit from the Bermuda holdings? (Q527, Fiona McTaggart)*

During the hearing, several Members suggested that shareholders only benefit if Google pays dividends back to shareholders. This is not the case. Google Inc has not paid dividends to shareholders at any point in the past and we have no current intention to do so. The funds held can be used to expand Google Inc's business operations outside of the U.S, which should in turn benefit Google's shareholders.

2. *Do you use other tax havens eg Bahamas, Cayman islands, Netherlands Antilles? (Q528–531 Chair)*

No.

3. *Please provide details of the costs involved in your operation in the UK (Q559–565, Richard Bacon)*

Note 3 of the statutory audited financial statements of Google UK for 2011 contains a breakdown of administration expenses. Note 6 contains a further breakdown of staff costs. The breakdown of the administration expenses included in the financial statements is as follows (all in GBP):

Advertising and promotion expenses	105m
Professional services	10m
Auditor remuneration	55k
Stock based compensation expense	51m
Depreciation and amortisation	6m
Employee benefit expense	190m
Other administration expense	54m

4. *Please provide information on any royalties paid from Ireland (Q566–567, Stephen Barclay)*

Google Ireland Holdings pays royalties back to Google Inc. in the U.S. for the rights to use technology that has been added to the Google portfolio through acquisitions (eg YouTube). For the first three quarters of 2012, this sum was US\$200 million.

5. *How was the amount of tax paid on your foreign income reached? (Q 568–573, Stephen Barclay)*

Google pays all the tax it is required to pay in the UK and in every other country in which we operate. In the UK this included over GBP10 million of corporation tax and close to GBP50 million of employee taxes in the last three years. The US\$248 million tax we paid on foreign income that the question referred to relates entities throughout the world other than Google Ireland Holdings. Google follows the principles of international taxation in that taxes are paid based on where products are created rather than where they are consumed

6. *Are there any outstanding issues with HMRC about your accounts? (Q593 Chair)*

There are no outstanding issues with HMRC about Google UK's accounts. HMRC are currently carrying out a review of the tax returns filed by Google UK for 2005–2011 inclusive. This is standard practice and we are co-operating fully with that review.

7. *Do you think the OECD definition of what a 'branch' is should be updated for the internet world? (Q605, Meg Hillier)*

Google UK Ltd provides sales, marketing and R&D support to Google Inc. It is paid for those services by Google Inc (in respect of R&D) and Google Ireland (in respect of Marketing and service support) and, in doing so, receives a profit that is equal to what other companies would get for performing the same activities. This relationship would not be affected by any changes to the definition of a "branch."

8. *Do you know how much you spend on tax lawyers and details of any external advice you seek? (Q 607-610, Meg Hillier)*

As with all large corporations, we use outside tax attorneys to consult on various tax issues. We do not have a full breakdown of those costs across all jurisdictions.

21 November 2012

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