Tax and our total contribution to public finances

This is our third transparency report setting out Vodafone's contribution to public finances in the countries in which we operate. This report has been updated to incorporate financial data for the fiscal year ended 31 March 2014, presented – as in previous reports – on an actual cash paid basis rather than a statutory reporting basis to provide the clearest possible insight into the scale of money flowing from Vodafone to governments.

We have retained much of the explanatory text used in previous editions of this report to continue to provide an insight into our views on matters of public debate. Regular readers may therefore recognise certain sections of this report. We have also provided new or expanded commentary on multinationals and governments, our Luxembourg subsidiaries and our views on the G20/OECD Base Erosion and Profit Shifting (BEPS) initiative in light of continuing interest in those topics.

In preparing this report, we met a number of stakeholders with a specialist interest in tax transparency, including several international NGOs with active campaigns focused on this issue. We are grateful for their insights and suggestions. Some of these are reflected in this year's report; others will be considered for incorporation in future reports, including full narrative reporting on a country-by-country basis with any appropriate addition of further relevant financial metrics.

Total contribution: £14.75 billion

In 2013/14, Vodafone contributed £14.75 billion in cash to the public finances in our countries of operation, up from £13.5 billion in 2012/13. This includes a year-on-year increase of more than £300 million in direct taxes paid to European governments and an increase of nearly £1 billion in government revenues in the AMAP region from non-taxation-based sources such as spectrum fees. Direct taxes paid by our non-operating company businesses also increased by almost £2.7 billion year-on-year predominantly as a consequence of the Verizon Wireless transaction which concluded in February 2014.

Background to this report

The amount of tax paid by large companies continues to be a matter of significant public debate and scrutiny.

While individuals and companies have legal obligations to pay tax, those obligations do not, however, extend to paying more than the amount legally required. Companies also have a legal obligation to act in the interests of their shareholders; and Vodafone's shareholders include many of the investment funds relied upon by tens of millions of individual pensioners and savers.

At the same time, individuals and companies must meet their responsibilities to contribute to the funding of public services and infrastructure, without which societies cannot operate effectively. Achieving a transparent and effective balance between those obligations and responsibilities therefore remains integral to operating sustainably.

When considering a company's tax contributions, there are several important factors to take into account.

- In many countries and for many companies, **corporation tax payments only account for a small proportion of businesses' total tax contribution to national governments**. For example, corporation tax accounts for only around 8% of total tax paid to the UK Exchequer and just 23% of total taxes paid to the UK Exchequer by the UK's largest 100 companies[1]. Businesses also pay a very wide variety of additional taxes: as the Appendix (see page 13) demonstrates, corporation tax is only one of 60 different types of taxation paid by Vodafone's operating businesses every year.

[1] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/376863/20141112_Octreceiptsbulletin.pdf and http://www.pwc.co.uk/total-tax-contribution-100-group/index.jhtml

- **Corporation tax is paid on profits, not on revenues.** If a company makes little or no profit – for example, as a consequence of declining sales, competitive market conditions or a period of intense capital investment, particularly if funded through borrowing – it will generally incur lower tax charges than another similar company with higher profits. This approach is common to all countries as without it, companies enduring periods of low profitability would be faced with disproportionate tax demands and significant disincentives for investment in infrastructure. In a number of countries where we operate – including and particularly in the UK – the cost of acquiring radio spectrum from the government, high operating costs, substantial levels of capital expenditure and sustained competitive and regulatory pressures have a significantly negative effect on the profits of our local businesses. In addition, in some markets, other taxes that are levied on revenue (together with non-taxation-based contributions such as spectrum fees) have the effect of depressing profit and so reducing corporation tax liabilities.
- **Taxation is local.** Taxes generally fall due wherever profits are generated, and the tax liabilities that arise as a result are decided under the rules of the country that is host to the business in question. So, for example, a company operating in South Africa pays taxes to the South African government under tax rules determined by that country's government; and a company operating in Italy pays taxes under Italian rules to the Italian government. Vodafone pays all taxes due under the law in all our countries of operation: in 2013/14, these direct taxes paid amounted to more than £7 billion, an increase of over £2.8 billion on the total paid in 2012/13 which predominantly arose as a consequence of the Verizon Wireless transaction discussed later in this report (see section on Verizon on page 8). For further details, see section on 'Multinationals, governments and tax' on page 3.
- **Taxation is not the only route used by governments to raise revenue from businesses.** Governments also use other mechanisms to derive revenues from business activities, including a wide range of licensing regimes, revenue or production-sharing agreements and, for communications companies, radio spectrum fees and auction proceeds. These additional sources of government revenue are often substantial - sometimes exceeding the monies raised through taxation - and therefore represent a critically important contribution to public finances. It is therefore essential to take those government revenue-raising mechanisms into account when assessing the extent to which a company is playing its part in funding wider civil society. In 2013/14, cash revenues from Vodafone to governments from non-taxation-based sources exceeded £1.9 billion. While this was £1.3 billion lower than the figure for 2012/13, as the prior year included substantial (and costly) spectrum auctions in a number of Vodafone countries, these non-taxation-based revenues remain an important factor when evaluating Vodafone's total economic contribution.
- **Large companies are an important source of investment and employment.** Governments seeking to stimulate investment often develop corporate taxation regimes which are intended to attract the capital necessary to deliver key policy objectives. Those measures also aim to stimulate job creation, in turn leading to higher government revenues from employment taxes and increased levels of consumer spending on the part of an expanded workforce. This is particularly relevant when considering multi-billion pound, multi-year programmes to build critical national infrastructure, such as the UK government's target for universal broadband coverage by 2015 or the European Union's target for the entire EU to have access to broadband above 30 megabits per second (Mbps) by 2020. For context, over the last five years, Vodafone has invested (including spectrum) more than £18 billion across Europe, including more than £4 billion in the UK alone. Political leaders make an active choice to incentivise corporate investment by offering capital allowances – to be offset against future corporate tax liabilities – in order to achieve a wider national benefit that would otherwise have to be funded directly by the state, invariably through public borrowing. These allowances are deliberate design features, not 'loopholes': they reflect the public policy choices made by governments and also – wholly intentionally – have the effect of reducing tax liabilities for companies whose investment decisions support those policy choices. In 2013/14, capital investment (excluding spectrum) across our businesses increased by more than £1.2 billion to reach a total of £7.5 billion, including an increase of more than £1 billion across our European markets.

IN FOCUS: Multinationals, governments and tax

It is important to note that many governments methodically and purposefully shape their taxation regimes in order to compete with other countries in attracting international businesses and capital to their country and thus in turn stimulate job creation and skills development. Governments also use tax rules to incentivise (or disincentivise) a wide range of activities and behaviours across society as a whole. Tax regimes are therefore creatures of politics as much as economics and are modulated each year by elected representatives in national parliaments to achieve specific policy objectives.

At the same time, governments also choose to enter into pan-regional cooperation agreements designed to enable companies to establish operations in different countries and to operate and trade across borders with as few impediments as possible. For example, the free movement of capital, goods, services and people across borders has been one of the founding principles of the European Union since the Treaty of Rome came into force in 1958.

Multinational companies such as Vodafone therefore operate in an international taxation environment which is determined by governments working individually and collectively and which – in democracies – is ultimately shaped by voters. If governments are uncomfortable with the outcomes achieved from the laws they have created or inherited on assuming office, it is wholly within their power to change those laws. This means we have to deal with different laws in the different countries we operate in; those laws are not always coordinated and can occasionally give rise to 'double taxation'.

A number of campaigners on taxation issues have alleged that in practice 'there is one set of rules for multinationals, another for everyone else'. This is untrue. Larger businesses are more complex, which in turn means a greater level of complexity in applying the rules. But they are the same rules. Similarly, while large companies may occasionally be consulted on how tax rules should change – a topic we discuss below (see section on 'Contributing to the development of tax policy' on page 6) – there is no certainty whatsoever that their views (or the views of any other interested party responding to a government consultation) would be taken into account when policymakers determine the rules to be applied in future.

As an international business, Vodafone – in common with all multinational companies – chooses from a range of locations when setting up certain centralised global operations such as procurement or IT support. Our decisions are influenced by a wide range of factors beyond the local tax environment, including:

- the stability and predictability of the political, regulatory and social environment, including respect for the rule of law and compliance with international human rights conventions;
- the availability of relevant skills within the local labour force;
- labour costs and the cost of operations;
- the effectiveness of transport links;
- the quality and reliability of communication networks; and
- the range and cost of commercial real estate.

In an international context, various treaties and inter-governmental agreements ensure multinational companies are not subject to 'double taxation' by paying tax twice over in two different countries in relation to the same economic activity. Governments also maintain measures that restrict companies from entering into artificial arrangements to move profits from one country to another lower-tax destination. We would emphasise that it is our policy not to enter into artificial arrangements[2] – for example, by artificially diverting profits to minimise tax payments to the UK Exchequer - and will only adopt business structures that reflect genuine and substantive commercial and operational activities.

Governments generally also require multinational companies to apply 'transfer pricing' rules to inter-company activities to ensure that profits are allocated to the countries where the relevant economic activity takes place. Vodafone has a number of centralised global functions located within specific countries, all of which operate in accordance with OECD best-practice transfer pricing rules. For example, the intellectual property associated with the Vodafone brand is held in the UK and the team of brand and marketing professionals responsible for the strategic international development and deployment of the Vodafone brand is based in London. There are therefore transfer pricing arrangements in place under which our operating companies around the world pay an 'arm's-length', externally benchmarked and verified, royalty fee to a UK-based Vodafone Group company for use of the Vodafone brand.

We have also established international IT and back office support hubs in countries including Germany, Ireland, Hungary, Romania, India and Egypt, and we provide insurance services from our regulated businesses in Malta, all of which operate under similar transfer pricing arrangements. The same rules also apply to our global subsidiaries based in Luxembourg, as explained below (see section on Luxembourg on page 4).

[2] See the tax risk management policy for more information http://www.vodafone.com/content/dam/sustainability/pdfs/vodafone_tax_risk_management_strategy.pdf

IN FOCUS: Vodafone, Luxembourg and 'tax havens'

As we explain above (see section on 'Multinationals, governments and tax' on page 3), many governments seek to develop tax regimes which provide some form of competitive advantage when seeking to attract inward investment from multinational companies that would otherwise flow towards other countries. As a consequence, variations have emerged between the tax regimes of different countries over the years, and some countries where specific aspects of the national tax regime offer significant advantages to businesses located there have found themselves dubbed as 'tax havens'.

There are a number of different definitions of the term 'tax haven'. At its simplest, the term is relative: if the tax regime in Country A has a lower headline or effective tax rate than County B, then through the eyes of the people of Country B, Country A could be considered to be a 'tax haven'.

Most governments – including all EU Member States and international organisations such as the OECD - respect national parliamentary sovereignty in tax matters and recognise that there is a clear difference between fair tax competition focused on the rates and scope of taxation and tax practices which discriminate in favour of specific companies or which cause harm to the wider economy.

For example, many observers believe it is perfectly legitimate for the UK government to have a long-standing policy which enables multinational companies to claim debt interest relief (within complex and strict parameters) on capital raised from financial institutions to fund their international operations and to set this off against the profit from their UK operations. This policy is a distinguishing feature of the UK tax system. It provides a significant incentive for a multinational company to expand and finance its international operations using capital raised in the UK – and, often, to locate much of its international headquarters activity in the UK – rather than in another country. The policy also encourages smaller enterprises and entrepreneurs to expand overseas.

A more nuanced definition of the term 'tax haven' focuses on national tax policies which have the effect of incentivising activities that are ring-fenced from the local economy, may be specific to individual companies rather than available to all market participants and may be largely artificial in nature and designed purely to minimise tax. It is our policy not to enter into such artificial arrangements.

One country which has been the focus of public and political scrutiny in recent years is Luxembourg. While Luxembourg has been commonly described as a 'tax haven' by tax campaigners, this is a country in which Vodafone has a meaningful presence and which therefore plays a material role in any assessment of our overall contribution to public finances.

Our Vodafone Luxembourg subsidiaries are not 'brass plate' activities. These are substantive businesses employing around 300 people in our Luxembourg headquarters building. Our colleagues in Luxembourg manage the financing of many of our international operating companies, providing loans on a commercial 'arm's length' basis which reflect the costs of borrowing from an external bank in line with international best practice. Our Luxembourg-based global purchasing organisation - the Vodafone Procurement Company (VPC) – oversees more than €13 billion of global purchasing contracts. Our international roaming team are also based in Luxembourg, where they manage 627 international roaming agreements that enable Vodafone customers to communicate when travelling across more than 190 countries.

In common with any other European Union member state, the Luxembourg tax regime is defined in legislation which is approved by elected members of the national parliament. The country's tax rules are largely in line with those of many other member states, including a standard corporate tax rate of 29.22% (which is higher than the rate in a number of other EU member states, including the UK).

However, the Luxembourg tax regime has a number of distinguishing features within the country's standard national tax code that are typically drawn from competitive best practice in a number of EU member states. One of these features is particularly significant from Vodafone's perspective. Under long-established Luxembourg tax rules, a reduction in the book value of a company's assets (also known as an impairment or writedown of goodwill) that has been verified by independent auditors and the local tax authorities is recognised as a tax loss that can be offset against profits. This means that if a multinational company with a presence in Luxembourg acquires another business but then sees the value of that acquisition reduce as a result of deteriorating market conditions or performance, the difference between the acquisition cost and the 'mark to market' contemporary value of the acquired business – and the loss consequently realised by shareholders – is treated as a loss for tax purposes.

The logic behind this aspect of the Luxembourg tax regime is clear. If a company used €5 billion of its shareholders' funds to acquire a business that is later valued at €3 billion, the effect from the shareholders' perspective is €2 billion of value foregone. It may be a 'paper loss' – at least, up until the point where the company seeks to liquidate the asset – but for shareholders it is unquestionably a loss nevertheless.

Similar rules were in place in Germany 14 years ago when Vodafone acquired the Mannesmann conglomerate in 2000. That acquisition was followed by the dotcom crash, wiping tens of billions of euros off the value of the former Mannesmann business, resulting in significant losses for the Luxembourg subsidiary involved, and ultimately for all of Vodafone's shareholders.

Continued

As explained above, those historical losses can be offset against profit within our Luxembourg subsidiaries and are therefore utilised across the various Luxembourg business units also summarised above. During 2014, we recognised a large proportion of these historical losses in the form of deferred tax assets – totalling £22.6 billion – as at 30 September 2014. These were recognised as a consequence of the Verizon Wireless transaction, discussed later in this report. Deferred tax assets represent the amount of tax a company does not anticipate having to pay in future years, in a particular jurisdiction – Luxembourg, in this case – as a result of circumstances which have already occurred in the jurisdictions where these assets arise. We anticipate that it would require up to 60 years to utilise these assets.

In recent months, there have been a number of allegations of illegal state aid under which governments in a number of jurisdictions – including Luxembourg – have been accused of entering into special agreements with individual multinational companies that have the effect of reducing those companies' overall tax charge beyond the levels possible under the standard tax regimes in those jurisdictions.

Vodafone has not entered into any such alleged special agreements with the Luxembourg tax authorities. We have received 'advanced tax agreements' from the authorities in order to confirm that the standard provisions of the Luxembourg tax regime apply to our facts and circumstances. Agreements of this kind are standard practice in many countries: whenever there are complex transactions, unclear tax regulations or substantial values involved, tax authorities generally seek to provide companies of all sizes with both formal and informal rulings and clearances in order to reduce uncertainty. The 'advance tax agreements' in the Grand Duchy therefore do not in any way amount to any form of bespoke arrangement with, or preferential treatment from, the Luxembourg tax authorities.

Finally, it is important to note that changes to the UK Controlled Foreign Company rules introduced in 2013 mean that a proportion of profits from our Luxembourg subsidiary's global financing activities are also taxable in the UK. Further information on Vodafone and UK corporation tax is set out on this page.

IN FOCUS: Why does Vodafone pay little or no UK corporation tax?

As we explain on page 2, all over the world, governments are seeking to encourage companies to create jobs and build infrastructure by developing a range of tax incentives to attract new capital investment. The UK is no different.

Vodafone makes huge investments in the UK. We spent over £1.3 billion in 2013/14 – up from just over £1 billion in 2012/13 – building and upgrading the networks relied upon by millions of UK consumers and businesses. We have also paid the UK government more than £7 billion for our UK radio spectrum licences. We raised the money for those licences from UK banks and capital markets and we're now paying more than £600 million a year in interest costs on our overall UK borrowings to UK banks and financial institutions.

As the UK Government wants to encourage more investment in the UK's infrastructure and job creation, it allows all businesses to claim tax relief on the cost of the assets used in the business against their profits, when determining their corporation tax bills. The government also provides relief to all businesses for the cost of interest on their debts to UK banks and financial institutions. These allowances and reliefs are intentional, long-established and carefully considered: they reflect deliberate policy decisions by successive UK governments and are a cornerstone of UK taxation policy. Vodafone is no different to any other UK business, whatever its size: if a self-employed trader buys a new computer or a large UK business borrows money to build a new warehouse, exactly the same rules apply.

As we explain above, corporation tax is charged on profits, not revenues. The UK is an expensive and highly competitive country in which to do business and has one of the least-profitable mobile markets anywhere in the world. Many people confuse revenues with profits. However, our UK profit is a small fraction of our gross UK revenues; below £200 million in 2013/14, which is significantly less than the interest costs on our UK debt and is just over one-seventh of the amount of our annual UK capital investment programme.

Vodafone's UK corporation tax position is therefore determined by UK capital allowances for UK investment and UK debt interest relief on borrowings from UK banks and financial institutions, set against a (relatively very low) level of UK profit. As we explain above (see section on 'Multinational, governments and tax' on page 3), our overseas financing subsidiaries have no bearing on our UK corporation tax position and we do not artificially transfer profits to minimise tax payments to the UK Exchequer.

Finally, as explained on page 2, UK corporation tax accounts for a small proportion of the total taxes paid by UK businesses. In 2013/14, we paid the UK government £355 million in direct taxes – up from £275 million in 2012/13 – and, as we show in the table on page 10, our total cash contribution to the UK Government was over £1 billion.

Tax conduct and principles

We are committed to acting with integrity in all tax matters. We always seek to operate under a policy of full transparency with the tax authorities in all countries in which we operate, disclosing all relevant facts in full, while seeking to build open and honest relationships in our day-to-day interactions with those authorities, in line with our Tax Code of Conduct, which is contained within our Tax Risk Management Strategy[3].

In forming our own assessment of the taxes legally due for each of our businesses around the world, we follow the principles stated in our publicly available Tax Risk Management Strategy[3]. We have two important objectives: to protect value for our shareholders, in line with our broader fiduciary duties; and to comply fully with all relevant legal and regulatory obligations, in line with our stakeholders' expectations.

However, tax law is often unclear and subject to a broad range of interpretations. Furthermore, the financial affairs of large multinational corporations are unavoidably complex; we typically process and submit more than 12,000 tax returns to tax authorities around the world every year. The assessment and management of tax uncertainty is therefore a significant challenge for any company of Vodafone's scale, and the key issues are subject to review by the Board and Audit and Risk Committee.

Our overarching approach is to pursue clarity and predictability on all tax matters wherever feasible. We will only enter into commercial transactions where the associated approach to taxation is justifiable under any reasonable interpretation of the underlying facts, as well as compliant in law and regulation. Our tax teams around the world are required to operate according to a clearly defined set of behaviours, including acting with integrity and communicating openly. These are aligned with the Vodafone Group Code of Conduct and the values set out in The Vodafone Way.

Contributing to the development of tax policy

When governments seek to develop or change tax policy, they invariably seek input from a wide range of interested stakeholders, including business advocacy groups and a large number of individual companies. Vodafone regularly engages with governments – typically through public consultation processes or in our role as a member of an industry group – to provide our perspective on how best to balance the need for government revenues from taxation against the need to ensure sustainable investment.

We are active participants in the tax policy committee of the European Telecommunications Network Operators' Association (ETNO) and the Groupe Speciale Mobile Association (GSMA), which represents the industry when looking at emerging issues across the EU. In this role, we have shared our insights as a multinational operator with the European Commission Taxation and Customs Union Directorate-General (TAXUD). We are also one of the few companies in Italy to enter into the new co-operation compliance mechanism with the Italian Ministry of Finance and are active participants in the tax policy committees of Assotelecomunicazoni and the Confindustria Digitale in Italy.

We contribute to the tax committees of telecommunications industry organisations in Germany which work on legal developments with tax policy and on tax administration, including the interpretation and application of tax law. In the UK, our Group Chief Financial Officer is a leading industry representative in the government's Business Forum on Business Tax and Competitiveness, which aims to establish a more competitive UK tax system. Vodafone is also a member of the Cellular Operators Association in India.

We are members of the South African Institute of Chartered Accountants (SAICA) tax committee, which engages on a wide range of tax issues. We are also active participants in the African Industry Forum and are involved in the Mobile Operators Association of Tanzania, which lobbies on telecoms and general tax reform in the country.

IN FOCUS: Vodafone and the OECD BEPS project

In 2013, the Organisation for Economic Cooperation and Development (OECD) began work on the 'base erosion and profit-shifting' (BEPS) initiative. 'Base erosion' is the term used to describe the reduction in a country's overall tax revenues as a consequence of the fluid movement of corporate activity and funds between different jurisdictions. 'Profit-shifting' is the term used to describe the artificial arrangements which move corporate profits from one jurisdiction to another lower-tax jurisdiction.

The BEPS initiative was developed in response to public concern about the integrity of national and international taxation systems in an ever more complex global economy. It is likely to change national and international tax rules dramatically, leading to a new set of standards for international cooperation and transparency, as well as an increased level of disputes on the allocation of taxing rights between countries.

Vodafone has long demonstrated its commitment to transparency through publishing details of its Tax Code of Conduct, Tax Risk Management Strategy and, more recently, this report. We welcome initiatives to increase transparency in this critically important area of public policy and support measures to eliminate artificial profit shifting and unfair tax competition.

We continue to engage constructively with the OECD both directly and through our membership of bodies such as the Technical Advisory Group on the Digital Economy, the Confederation of British Industry, the 100 Group and the International Alliance for Principled Taxation.

Our focus is to support the OECD in developing practical and workable recommendations that support international trade, incentivise greater investment in infrastructure and services, foster economic growth, employment and prosperity and generate greater public trust in the international tax system.

The UK government has announced its intention to implement the OECD's recommendations regarding country-by-country reporting. These will require companies to report certain information to the UK tax authorities on a country-by-country basis, complementing Vodafone's ongoing commitment to tax transparency and country-level disclosure as exemplified by this report.

[3] http://www.vodafone.com/content/dam/sustainability/pdfs/vodafone_tax_risk_management_strategy.pdf

IN FOCUS: India and tax

In 2007, Vodafone, through one of its Dutch companies, purchased an indirect stake in a company in India from Hutchison Telecommunications International Limited. After the acquisition was completed, the Indian tax authorities sought to raise a tax demand against Vodafone, even though the transaction took place outside India between two non-Indian entities and Vodafone was the buyer, not the seller.

The Indian tax authorities' actions led to a protracted legal dispute, which culminated in a hearing before the Indian Supreme Court. The Supreme Court examined all the facts related to the transaction before concluding unambiguously and unanimously, in January 2012, that no tax was due. The Court also highlighted that it was important for the Indian government to avoid penalising international investment in the country.

Although the country's highest court had vindicated Vodafone's position, the Indian government subsequently changed the law to introduce retrospective taxation rules. Those rules, which were back-dated to 1962, were designed to require taxes to be paid retrospectively which, as the Supreme Court had concluded, could not be levied against Vodafone under any reasonable interpretation of the evidence or the law.

All businesses depend on tax policy predictability and certainty in order to plan investments for the long term. The Indian government's decision to rewrite half a century of tax legislation with immediate retrospective effect was widely condemned worldwide, greatly damaged global business confidence in the Indian government and led to a marked reduction in the flow of investment into the country.

As a result, the Indian government commissioned an independent inquiry, led by the economist Parthasarathi Shome, to recommend a way forward. The Shome Committee concluded that retrospective tax rules should be introduced only in the 'rarest of rare' cases, and that, if applied to capital gains tax cases, the authorities should pursue the seller, not the buyer (Vodafone being the latter not the former in the case at issue).

We continue to maintain that no tax is due on the 2007 acquisition and, despite constructive discussions with the Indian government regarding options for conciliation, were unable to agree on a way forward with conciliation. On 17 April 2014, we therefore filed our notice of arbitration under the bilateral investment treaty between the Netherlands and India (the Bilateral Investment Promotion and Protection Agreement) in an effort to resolve the dispute. Since then, both the Indian government and Vodafone have appointed arbitrators; however, we have yet to agree on a third arbitrator who would be the chairman of the international tribunal.

Meanwhile, in October 2014 the Bombay High Court ruled in favour of Vodafone in separate cases focused on whether or not the Indian tax authorities were correct in their pursuit of tax charges associated with the issue of shares from our Indian subsidiary to an overseas parent. The Court supported Vodafone's contention that the issue was not taxable as it had no impact on income, and in January 2015 the Indian government announced it would not appeal the Bombay High Court's ruling.

Vodafone has become one of India's largest investors: we have spent more than £12.8 billion in building our business in the country since 2007. We are also one of the country's largest taxpayers: as we set out under our country-by-country total contribution table (see the table on page 10), in 2013/14 our direct and indirect contributions to Indian public finances exceeded £2.2 billion.

IN FOCUS: The HMRC/Vodafone Controlled Foreign Companies settlement

In 2010, Vodafone and Her Majesty's Revenue and Customs (HMRC) concluded a long-running legal dispute focused on a specific point of UK and European tax legislation with a full and final settlement of £1.25 billion.

The background to this settlement is highly complex. It was focused on an area of law whose application was unclear and which successive UK governments agreed needed to be rewritten. It involved nine years of legal argument, three court cases and two independent appeals, followed by a detailed HMRC review and settlement in 2010. That settlement was then followed by a National Audit Office (NAO) inquiry in 2012, assisted by a former High Court judge, Sir Andrew Park. The NAO report concluded that the HMRC/Vodafone settlement was a good outcome for the UK taxpayer and that if Vodafone had chosen to continue litigation instead of settling with HMRC "there was a substantial risk that the Department [HMRC] would have received nothing".

The dispute focused on the UK tax authorities' interpretation of Controlled Foreign Companies (CFC) legislation and began when Vodafone bought the Mannesmann conglomerate in Germany in 2000. The acquisition was largely for shares and involved no borrowings or loans from Vodafone's UK business. Importantly, there was no reduction in Vodafone's UK tax contributions as a consequence, and the dispute was not related in any way to the tax liabilities arising from our UK operations. We therefore questioned the UK tax authorities' application of the rules on both factual and legal grounds, in common with a number of other companies who had also challenged the UK's approach to CFC legislation.

As explained above (see section on Luxembourg on page 4), Vodafone's subsidiary in Luxembourg is the main financing company for our many operations around the world. The UK tax authorities argued that, had those financing activities been established and undertaken in the UK, they would have attracted tax in the UK, and that therefore tax should be payable under UK CFC provisions. Vodafone argued that, as a matter of European law, we were freely entitled to establish activities wherever we chose, and that as a matter of fact, these were neither artificial arrangements nor did they have any impact on Vodafone's UK tax liabilities.

The underlying facts were scrutinised by the UK tax authorities and the points of law involved were examined in detail by the European Court of Justice, the UK High Court and the UK Court of Appeal, prior to the decision to reach a settlement. Subsequently, the UK Government sought to address a number of inconsistencies and flaws in UK CFC legislation, clarifying the UK's approach to this complex area of international taxation in new rules which took effect in January 2013.

IN FOCUS: Verizon Wireless

In February 2014, we completed our sale of our US group, whose principal asset was Vodafone's 45% shareholding in Verizon Wireless, to our US joint venture partners, Verizon Communications Inc., for a total consideration of $130 billion.

Our US group structure was predominantly a legacy of prior mergers and acquisitions dating back more than 14 years. In addition to the Verizon Wireless shareholding, our US group also owned a range of minority non-US interests acquired in the merger with AirTouch Communications Inc. in 1999 together with other non-US interests acquired over time.

It would not have made sense to leave those legacy non-US interests (which were not included in the sale to Verizon Communications) stranded in US jurisdiction once the sale of our US group was completed. We therefore undertook a rationalisation and reorganisation of the US group structure prior to completion of the transaction to ensure that those non-US interests were held by Vodafone outside the United States. That reorganisation gave rise to an estimated £2.2 billion US tax liability under standard US tax rules; a sum which was paid to the US tax authorities in 2014.

Our US group has always been owned by one of Vodafone's European holding companies, based in the Netherlands, which also own many of our other international assets. Our European holding company sold the US group to Verizon Communications in its entirety once the rationalisation and reorganisation, described above, had been completed.

The sale of our US group was not taxable under standard US tax rules: under the US tax code, US tax is not imposed on these types of sales of shares by non-US-based entities. Such treatment is also consistent with US tax treaties. The sale was also not taxable under standard Dutch rules: long-established tax law in the Netherlands provides a participation exemption on dividends received and capital gains arising from the sale of shares by any Dutch company, whatever the size of the company or the size of the transaction involved. A number of other EU countries have similar provisions in place, all of which are designed to stimulate long-term corporate investment and consequential broader benefits for the wider economy.

While the UK is not a relevant jurisdiction for tax purposes given the locations of the buyer (the United States) and the seller (the Netherlands), under rules established in 2002, the UK has similar shareholding disposal exemptions to those of the Netherlands.

Our contribution, country by country

Vodafone plays an important role in contributing to the economies of the countries in which we operate. We are a major investor, taxpayer, employer and purchaser of local goods and services. We also make a vital contribution to the delivery of governments' policy objectives through our substantial capital expenditure in building the next generation of digital infrastructure.

We contribute directly to public finances through a wide range of taxes, as well as non-taxation revenue mechanisms, such as spectrum licences and regulatory fees. We also make a significant indirect contribution through the taxes paid by our employees and the suppliers that our businesses support (many of which are dependent on our business), as well as through taxes collected on governments' behalf, such as sales taxes and VAT.

Assessing our contribution to public finances

The table below sets out the data for five of the most relevant indicators of Vodafone's total overall contribution to the public finances and wider economies of the countries within which we operate.

To ensure the most effective comparisons between different types of contributions are within the same period, all the data presented in the table below is for the 2013/14 financial year and is drawn from our audited accounts.

In the 2013/14 financial year, Vodafone's businesses around the world paid more than £7 billion in direct taxes to governments in our countries of operation plus more than £1.9 billion in other non-taxation-based fees and levies. Our businesses also made a total indirect tax contribution to national governments of £5.8 billion. Our total cumulative contribution to the public finances of our countries of operation was therefore £14.75 billion. We also invested more than £7 billion in the networks and services now relied upon by more than 438 million mobile customers and 11 million fixed broadband customers worldwide.

In the table on page 10, the direct tax contributions to governments are reported on an annual actual cash paid basis for each local market as, in our view, these are among the most meaningful and transparent metrics to consider when assessing a company's tangible role in helping to fund public services. International accounting rules governing the reporting of a multinational company's profit and loss tax liabilities and charges are complex, reflecting a wide range of factors such as deferred taxation, losses, group-level taxation and various provisions related to uncertain tax positions. The cash payments or reliefs arising from those factors may be several years in the future. As a result, there can be a variance between a multinational company's statutory reported numbers over a specific time period – particularly in territories with holding companies as well as a local operating company – and the actual cash paid numbers set out below[4]. For more detailed information about our financial performance in 2013/14, see the Vodafone Group 2014 Annual Report and Accounts[5].

The columns in the table are explained below.

- **Direct government revenue contribution: taxation.** This encompasses Vodafone's total direct tax contribution in each country, including corporation tax, business rates or equivalent, employers' national insurance contributions or equivalent, municipal and city taxes, sector-specific taxes (such as 'special' taxes, 'telecoms' taxes or 'crisis' taxes), stamp duty land tax, stamp duty reserve tax, irrecoverable Value Added Tax (VAT), insurance premium tax, climate change levy, environmental taxes, customs duties, fuel excise duties and acquisition taxes. An illustrative list of the types of taxes paid is set out in the Appendix (see page 13).
- **Direct government revenue contribution: non-taxation mechanisms.** This encompasses all other forms of government revenue raised in addition to a country's direct taxation regime, including telecoms licence fees, radio spectrum management fees, proceeds from revenue-sharing agreements, usage fees and proceeds from radio spectrum auctions. Examples of these payment types are listed in the Appendix (see page 13).
- **Indirect government revenue contribution.** This encompasses taxes collected by companies on behalf of national governments, including Pay As You Earn (PAYE) income tax, employees' National Insurance contributions, withholding taxes, sales and consumption taxes and VAT. These indirect contributions to government revenue would not be collected (or generated to the same extent) if the company did not employ people and offer services or products to the customers responsible for paying the tax in question, or procure goods and services from its suppliers on which such taxes are due.
- **Capital investment.** Our significant investments in building the networks and services relied upon by more than 438 million Vodafone mobile customers around the world are often taken into account by local tax authorities when determining corporate tax liabilities.
- **Direct employment.** Vodafone is an important source of employment and skills transfer worldwide. We provided incomes, benefits and the potential for a high-technology sector career path for 92,812 people in more than 27 countries as of end March 2014 (2012/13: 91,272). In addition, we have contractual relationships with many thousands of suppliers and partner companies around the world, each of which relies to a greater or lesser extent on revenues from Vodafone to pay their employees' wages.

This data is intended to provide a broader insight into Vodafone's significant economic contribution to the societies in which we operate. We have no view on the merits of direct versus indirect taxation, nor on the distinction between the revenues that flow to governments from taxation versus those obtained through other means, such as spectrum fees. Governments – not companies – determine the rules.

[4] For example, see http://www.cbi.org.uk/media/2145560/making_the_case_-_july_2013.pdf

[5] http://www.vodafone.com/content/annualreport/annual_report14/downloads/full_annual_report_2014.pdf

The figures set out in the table below will vary widely from country to country and from year to year as a result of local differences between, and annual movements in, factors such as levels of profit and capital investment. There are also wide variations in local taxation regimes and other government revenue-raising mechanisms, many of which change from year to year. For example, non-taxation-based revenues will typically be very high in a year in which a government benefits from the proceeds of a spectrum auction (as happened in the UK and Netherlands in 2012/13) but much lower in a year where no such auction takes place. It does not make sense, therefore to try and compare the amount of tax or investment made in one country to another, given the factors described above.

Total Economic Contribution – country by country

	Direct revenue contribution: taxation		Direct revenue contribution: other non-tax		Indirect revenue contribution		Capital investment		Direct employment[6]	
	FY 13/14 £m	FY 12/13 £m	FY 13/14 £m	FY 12/13 £m	FY 13/14 £m	FY 12/13 £m	FY 13/14 £m	FY 12/13 £m	FY 13/14	FY 12/13
Europe										
Albania	5	4	1	1	14	16	25	20	399	420
Czech Republic	10	25	106	9	50	66	67	69	2,040	2,517
Germany	336	106	–	–	1,049	1,068	1,483	1,246	14,187	11,031
Greece	14	25	7	6	169	178	70	66	1,726	2,002
Hungary	14	43	3	61	92	70	45	52	2,616	2,351
Ireland	79	24	–	149	71	92	127	102	1,084	1,115
Italy	520	425	–	12	976	903	963	579	6,977	7,553
Malta	41	37	3	2	9	9	12	26	312	316
Netherlands	82	65	–	1,124	195	233	226	219	3,637	3,467
Portugal	47	65	7	7	115	133	155	129	1,426	1,484
Romania[7]	25	28	149	195	79	91	80	79	3,232	3,308
Spain	91	172	73	255	288	314	505	367	3,567	4,239
UK	355	275	24	825	630	776	1,310	1,076	12,979	13,479
Europe Total	**1,619**	**1,294**	**372**	**2,646**	**3,738**	**3,949**	**5,066**	**4,030**	**54,181**	**53,282**

Continued

Tax and our total contribution to public finances: Our contribution country by country

	Direct revenue contribution: taxation		Direct revenue contribution: other non-tax		Indirect revenue contribution		Capital investment		Direct employment[6]	
	FY 13/14 £m	FY 12/13 £m	FY 13/14 £m	FY 12/13 £m	FY 13/14 £m	FY 12/13 £m	FY 13/14 £m	FY 12/13 £m	FY 13/14	FY 12/13
AMAP Region										
Australia	6	7	201	26	32	33	255	281	1,651	2,060
DR Congo	26	23	19	16	30	25	57	49	645	606
Egypt	116	108	48	54	155	173	218	211	7,622	5,091
Fiji	0	2	1	1	2	2	3	7	127	120
Ghana	18	6	–	3	34	38	36	36	1,175	1,279
India	254	289	1,088	442	893	986	715	555	16,194	14,449
Kenya	118	80	6	8	20	18	80	12	1,334	1,071
Lesotho	3	5	2	2	2	1	11	8	150	123
Mozambique	3	1	2	–	3	4	78	47	337	284
New Zealand	23	46	9	1	81	78	146	117	3,450	3,271
Qatar	–	1	3	–	–	–	59	69	445	420
South Africa	330	375	19	20	261	318	430	506	4,886	5,118
Tanzania	65	42	10	8	48	40	88	92	509	480
Turkey	296	454	155	–	433	375	252	247	3,310	3,340
AMAP Total	**1,258**	**1,439**	**1,563**	**581**	**1,996**	**2,091**	**2,429**	**2,237**	**41,835**	**37,712**
Non-OpCo	4,141	1,466	0	2	65	38	16	11	948	977
Global Total	**7,017**	**4,200**	**1,935**	**3,229**	**5,798**	**6,078**	**7,510**	**6,278**	**96,964**	**91,971**

Notes:

The table above includes all contributions from countries within the Group's Europe and AMAP regions, as set out on page 5 of the Vodafone Group 2014 Annual Report and Accounts[8]. Non-controlled interests and common functions are included within the 'Non-OpCo' line, unless the contribution is from a country already listed in the regions above.

[6] The global total direct employment number includes employees in our non-controlled assets who are excluded from the numbers in the Vodafone Group 2014 Annual Report and Accounts[8] and excludes some roles in global functions which are included in the Annual Report[8]. The 2012/2013 direct employment numbers have been restated to include some Group function roles where we are able to allocate these to a specific jurisdiction. We have also restated the Italian 2012/13 direct employment number to reflect 100% ownership of Italy following our acquisition of the remaining 23% in February 2014.

[7] The direct revenue tax contribution: taxation for Romania has been restated to remove a number incorrectly included in the 2012/13 contribution.

[8] http://www.vodafone.com/content/annualreport/annual_report14/downloads/full_annual_report_2014.pdf

'Non-OpCo' includes (i) subsidiaries in countries where the Group does not have an equity interest in a company which holds a licence to provide mobile telecommunications services) and (ii) the US group which owned the 45% shareholding in Verizon Wireless prior to the sale of that group as explained earlier in the report.

'Non-OpCo' includes a direct revenue contribution of £5 million and an indirect revenue contribution of £64 million attributable to our activities in Luxembourg in 2014.

The source data is predominantly drawn from information included within the publicly available Vodafone Group 2014 Annual Report and Accounts[10], the public accounts of the Group's listed operating company subsidiaries and the accounts of various non-listed Group operating company subsidiaries.

The Vodafone Group public accounts are certified by the Group's external auditors and the public accounts of the Group's listed operating company subsidiaries are certified by those companies' external auditors. Additional data is subject to assurance by EY.

Key Vodafone Group financials and statistics at global level

	2013/14	2012/13
Revenue (£m)[9]	**43,616**	44,445
Adjusted operating profit (£m)[9]	**7,874**	12,577
Free cash flow (£m)[9]	**4,405**	5,608
Employees[9]	**92,812**	91,272
Market capitalisation (£m)	**58,300**	91,300
Group mobile customers (million)	**433.7**	403.9

[9] Values disclosed represent the management basis of presentation as restated in the preliminary results announcement for the year ended 31 March 2014. 2012/13 values have been restated.

[10] http://www.vodafone.com/content/annualreport/annual_report14/downloads/full_annual_report_2014.pdf

For more detailed information about our latest financial performance in 2013/14, see our Annual Report[10].

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This report is included within EY's specific tax assurance statement.

http://www.vodafone.com/content/dam/sustainability/2014/pdf/assurance_statement_tax_2013-2014.pdf

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Appendix: Taxation types

The table below provides an illustrative overview of the types of taxation paid by Vodafone operating companies around the world every year.

Direct taxation

Advertisement tax
Airtime excise tax
Business profits tax
Business rates
Capital gains tax
City services levy
Climate change levy
Commission levy
Communications services tax
Company car tax
Construction tax
Corporation tax
Crisis tax
Donations tax
Economic activity tax
Education tax
Employers' national insurance contributions
Employers Provident fund contribution
Environment tax
Environmental product fee
Expatriate tax
Fringe benefit tax
Fuel duty
Game tax
Garbage tax
Homologation tax
Import duty
Innovation contribution
Insurance premium tax
Interconnect tax
International inbound call termination surtax
Irrecoverable value added tax and goods and services tax
Judicial tax
Levy contributions
Local business tax
Minimum alternative tax
Mobile telecoms services value added tax
Mobile telecoms value added tax (higher rate)
Municipal and city rates
Municipal tax on immovable property
Municipal waste tax
National health insurance levy
Net wealth tax
Numbering tax
PAYE settlements
Railway development levy
Rehabilitation contribution
Social security tax
Special communications tax
Special consumption tax
Sprint payments
Stamp duty land tax
Tax on public domain/fixed lines
Tax on prize programmes
Technology tax
Transfer tax
Turnover tax
Universal service tax
Withholding tax
Workers' compensation insurance levy

Non-taxation-based fees

Annual government fee
Chamber of commerce fees
Identity management fee
International Mobile Equipment Identity (IMEI) number registration fees
Licence renewal fees
National Copyright Collecting fees
Network usage fees
Proceeds from revenue sharing agreements
Radio link fees
Spectrum auction receipts
Spectrum management fees
Telecoms levy
Telecoms licence fees
Usage fees
Wireless connection fees
Wireless usage fees