Submission to the House of Lords Economic Affairs Committee: Finance Bill Sub-Committee 2013

Countering the avoidance of tax

22 January 2013
About ICAS

1) The Institute of Chartered Accountants of Scotland ("ICAS") is the oldest professional body of accountants. We represent around 19,000 members who advise and lead businesses. Around half our members are based in Scotland, the other half work in the rest of the UK and in almost 100 countries around the world. Nearly two thirds of our members work in business, whilst a third work in accountancy practices. ICAS members play leading roles in around 80% of FTSE 100 companies. ICAS is also a public interest body.

2) ICAS welcomes the opportunity to comment on the legislative proposals to counter tax avoidance. ICAS considers taxpayers should pay the right tax at the right time, and that there is a timely need to consider both the legislative and administrative responses to the media, parliamentary and public discussions of tax avoidance.

Countering tax avoidance

3) ICAS recognises the need for a proportionate and effective anti-avoidance approach in UK tax law, applied consistently. This will support the Government's policy of deterring and countering tax avoidance, whilst retaining a tax regime that is attractive to business, in terms of certainty and practicality. The measures necessary in this approach are:

   a. Clearly written tax legislation, supported by policy statements as to its purpose and limitations, introduced after appropriate consultation. This applies to all new legislation, including any general anti-abuse rule.
   b. A definition of tax avoidance capable of operation and application at a practical and detailed level, giving clarity and certainty between what might be acceptable tax planning and what might be regarded as unacceptable.
   c. An experienced and effective compliance and enforcement operation in HMRC.
   d. A simpler tax system, with the minimum of rate differences, reliefs or exemptions, thus limiting the opportunity for tax avoidance.

4) A substantial part of media coverage recently has been in relation to international businesses, who are complying with UK legislation, in that they are applying transfer pricing principles to, for example, payments of royalties for the use of intellectual property rights. This is not tax avoidance that would necessarily be affected by the proposed general anti-abuse rule, discussed further below. It is also a consequence of seeking to make the UK a competitive place to do business; that is the context and balance to be considered even if some businesses UK corporate tax liabilities appear to give rise to concerns. If the UK government wishes to change core UK corporation tax principles, it would be preferable to do so after a proper and informed consultation process.

5) Where international businesses achieve tax efficiencies by structuring operations on a global basis, a correspondingly global approach would be needed to address these, and consider the tax arrangements that exist between different tax jurisdictions. In this the roles of the Organisation for Economic Cooperation and Development in joint international initiatives, and perhaps also the European Union, in its consideration of “double non-taxation” (gaps or mismatches between members countries’ tax systems) are likely to prove more effective than the UK acting on its own.
6) ICAS is generally supportive of the attempts by the Government and HMRC to seek a statutory solution to the tax avoidance issue and in broad agreement with much of the draft legislation. A number of concerns remain however where improvements are being sought; in particular that any provision should not be so vague that it could become a tool easily misused by HMRC.

7) ICAS supports the approach recommended by Graham Aaronson QC; that a general anti-abuse rule rather than a general anti-avoidance rule, is to be preferred. This is due to the difficulty recognised in achieving an agreed definition around measure 3(b) above, the fact that tax is a matter for legal interpretation, and in view of the policy aim of offering sufficient certainty to businesses.

8) ICAS consults regularly with HMRC’s anti-avoidance unit. Most recent discussions have been in relation to the 2012 Consultation Documents on the proposals for a general anti-abuse rule and revisions to the Disclosure of Tax Avoidance Schemes regime. Our aim, in the public interest, is to ensure such provisions are efficient and effective and do not place an unnecessary or disproportionate burden on compliant taxpayers and businesses.

The legislative proposals in the Finance Bill 2013

9) A general anti-abuse rule (“GAAR”)

The draft GAAR legislation was released in December 2012. In order to appreciate its impact and effectiveness, it must be read alongside the accompanying administrative package of HMRC’s draft GAAR Guidance. This comprises HMRC’s consultations drafts Part A; “Scope of the GAAR legislation”, Part B; “Examples of how the GAAR applies to Tax Arrangements”, and Part C; “GAAR procedure”. ICAS will be submitting consultation responses to HMRC on points of detail in these in due course but identifies below the key issues, which, read together, give concerns over the potential for lack of clarity and misuse of the legislation.

Our main concerns are:

a. The draft clauses do not establish an obligation to ensure the independence of the GAAR Advisory Panel. Whilst that panel will not include HMRC officials, such officials will be responsible for all appointments to the panel. The GAAR Advisory Panel is proposed as a key safeguard in the application of the general anti-abuse rule, and should be constituted accordingly. Other approaches to the obligations on members of the GAAR Advisory Panel, perhaps as for First Tier Tax tribunal members, might be considered.

b. The changing view on what is, or is not, acceptable tax planning, needs to be more protected, or legislative uncertainty may be created, due to the lack of clarity over the principles or policy objectives of older legislation. The current debate on tax avoidance demonstrates that the area of tax planning that is acceptable may be shrinking, yet there is little clarity on what governments or HMRC regard as unacceptable. The “will of parliament” and “spirit of the law” sentiments translate to the policy objectives provision in section 2(2) or the intended result of the provisions, included in section 2(4), but without appreciation of the difficulty that can arise in arriving at these intentions. A good example, relating to corporation tax losses, was revealed in the recent consultation on the Disclosure of Tax Avoidance Scheme rules. In that example, a targeted anti-avoidance rule prevented relief in some commercial circumstances, but not in others. The intention of parliament around these different circumstances is not clearly found at present, but given nearly twenty years of published awareness of the particular wording, with no indication of any concerns or counteractions from HMRC, it is difficult to conclude that a taxpayer arranging commercial activities to achieve that continuing relief in the present day, was undertaking objectionable tax avoidance.
c. However the view in b) above has been challenged by the 2012 HMRC Consultation Document updating the disclosure regime, when that example was described by HMRC as tax avoidance “other than benign”. The exclusion in section 2(5) where HMRC had “indicated its acceptance of that practice” is therefore too restrictive, and should be extended to include situations such as that in the example above, where tax planning was regarded as acceptable in wider published materials in the public domain, assuming of course no contrary indications of the position had been widely publicised by HMRC. This extension of section 2(5) reflects, and would be consistent, with the matters relevant to court or tribunal proceedings, in section 6(3).

d. The role of the GAAR Advisory Panel in expressing an opinion appears more limited than originally expected; an opinion notice need only specify whether the taxpayers steps were “a reasonable course of action” (schedule 1 paragraph (3)). In providing a vital safeguard to HMRC’s potentially extensive application of these provisions, it would be preferable for the opinion provided to be on whether the general anti-abuse provision, drafted in section 2, either applied, or did not apply. The GAAR Advisory Panel’s view should then explicitly be seen, as a “reasonable” one in the first of the reasonableness tests in that section. That view would be expected then to have considerable influence on HMRC’s decision on how to proceed; that is what provides the safeguard and is missing from the current draft.

It also has to be remembered that the GAAR Advisory Panel would, in due course, perform its second role of approving the GAAR Guidance. That is meant to indicate whether the GAAR would or would not apply to particular circumstances in advance, so consistency with the opinion role given after the event, on the same principles, would not appear unreasonable.

10) Cap on income tax reliefs

The policy intention cited for this proposal is “fairness”; it is not being introduced to target tax avoidance although it was recognised that it will reduce the scope for exploiting income tax reliefs for tax avoidance purposes.

Our observations on the effectiveness of this are:

a. In the context of “fairness”, a taxpayer’s ability to pay should also be taken into account. A taxpayer with two trades or businesses (or other income source), who had profit/income of say £70,000 and a loss in a start-up trade of, say, £90,000, would have an economic deficit but be taxed in that year on £20,000. The justification of fairness is therefore flawed in principle. This instrument is too blunt. It has adverse cash flow implications for genuine businesses and could inhibit business development, contrary to wider government objectives.

b. In the context of this hearing considering the approach to countering tax avoidance, this capping provision suggests the GAAR discussed above, together with existing targeted restrictions on the use of trade tax losses, and HMRC’s anti-avoidance efforts are not regarded as sufficient to have a meaningful impact on any abuse of tax reliefs from losses. If that is the case, it is the GAAR or existing targeted provisions that require revision; the case for this additional wide provision is questionable.

c. This restriction operates as an additional layer of complexity in computational matters, as demonstrated by the recognition in the “summary of responses” at paragraph 3.2 that extensive guidance and worked examples will be needed to support taxpayer compliance with the provisions. Instead of adding this layer of complexity, the GAAR should be allowed to operate as intended for the exploitation of reliefs in an abusive fashion.