Response from ICAS to the HMRC Consultation on a General Anti-Abuse Rule

14 September 2012
About ICAS

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.

General comments

ICAS welcomes the opportunity to contribute to the consultation on the matter of addressing artificial and abusive tax avoidance schemes through the proposed introduction of a General Anti-Abuse Rule ("GAAR"). We note the contents of the letter from Graham Aaronson to David Gauke on 27 June expressing support for the draft legislation attached to the consultation document. We also note that the study group in that letter did not address wider "middle ground" impacts of tax avoidance addressed in the consultation document, or the implementation issues and practicalities, which are key to business certainty as well as the effectiveness of these proposals, as a deterrent and countermeasure. The practicalities are the basis of many of the general comments below, where we also address the detailed questions in the consultation document.

The lack of detail on the Advisory Panel and the lack of draft guidance for consultation have an impact on our view on the clarity of, and timescale for, introduction of the legislation. It makes it impossible to conclude that an early effective date for the full legislative package would be wise. We would be happy to work with HMRC and policy makers towards completion of the package of measures which would achieve the policy objective in an effective manner.

Support for greater legislative clarity

We support the proposal that providing greater clarity around the intended policy objectives for this, and other, tax provisions should assist future judicial interpretation, and the effective application of the proposed GAAR. However it has to be accepted that this is not likely to address historic legislative weaknesses with unclear policy objectives.

We have called consistently for legislators to write tax legislation to achieve specifically the tax charges and reliefs Parliament intends should apply. Later developments or events may require legislation to be updated or adapted but best efforts and appropriate resources should still be dedicated to improving the quality of legislative drafting. Undertaking full and effective consultation prior to the introduction of new legislation is essential.

It has been suggested that for the GAAR, guidance approved by the Advisory Panel will provide practical information for taxpayers and a safeguard to certainty, but it is difficult to see the guidance as clarifying the intention of Parliament when it will have no Parliamentary scrutiny nor involve Parliamentarians; at best this is a delegated activity. Regardless, if it is to be a practical support and gain credibility and acceptability in practice, in support of certainty, it is suggested that that the detailed supporting guidance should not solely be drafted by HMRC but, in accordance with the government's consultation principles, be open to full consultation. That would permit proper debate, a balanced and informed output and minimise the practical uncertainty level for taxpayers as to what might be challenged, under the GAAR or otherwise.

It has to be remembered that the GAAR is a provision to tax what Parliament has failed to tax specifically, and a serious public commitment is needed from both Government, and HMRC, to ensure that it does not become a "catch all" provision for inadequate legislative efforts or failed administrative procedures. That safeguard is presently missing from the current proposals, but along with the safeguards called for around the guidance and the Advisory Panel below, is needed so that the GAAR does not become an easily misused tool in the fulfilment of the HMRC’s objective to close the “tax gap”, but maintains its more restricted policy objective.
Properly considered implementation plans are essential

Inadequate or poorly thought out procedures and processes, or poor implementation in practice of any GAAR legislation, could lead to even more complexity and uncertainty for taxpayers, especially businesses. ICAS believes that investment in the right staff at HMRC is needed to enforce existing legislation, to address illegal tax evasion and to support compliant taxpayers.

Considerable consideration still has to be given to operational issues and the practical workings of the proposed GAAR, from both a taxpayer and HMRC perspective. Behavioural consequences of these provisions are not explored at all in the document, beyond the intent that there will be a deterrent effect on artificial and abusive tax avoidance; commercial responses are not addressed further. However, experience dictates that major changes to the tax system have such effects, and these should be fully evaluated.

More is needed to avoid uncertainty

ICAS fully supports the principle that taxpayers should pay the right amount of tax, being the amount of tax payable according to tax legislation. There is an established legal principle, that a taxpayer need not deliberately pay the maximum amount of tax possible, but can arrange his or her affairs to manage tax costs efficiently, within the law. That is regarded as acceptable tax planning. Unacceptable tax planning is not specifically defined anywhere, so we have consistently called for the key preparatory step in tackling anti-avoidance to be to draw this “line in the sand”, and define “tax avoidance” and its relationship to “tax planning”. Despite the statement at point 2.5 of the document that “HMRC will challenge, and, where it can, counteract all forms of tax avoidance”, it has failed to define what that means in practice.

Arriving at a definition of tax avoidance is not easy, hence the policy intent behind the proposals under discussion are to address the extremity of artificial and abusive tax planning behaviour. Deterrence may be its greatest effect, but the legislative solution to counteract such behaviours is provided for.

We also note the policy intention was not to undermine certainty for taxpayers and businesses operating in the UK. Any uncertainty of tax outcomes is not good for economic activity and the risks of deterring commercial transactions, and not just favourable tax outcomes that may result, has to be properly managed. A failure by HMRC to define what tax avoidance it will attack, in a complex system such as in the UK, in itself causes uncertainty of tax outcomes and resolves little for the uncertain, but willingly compliant, taxpayer.

We are concerned that the proposals in this consultation document will not achieve the required level of certainty for taxpayers. The specific reasons for our concerns are under the following headings,

1. The lack of clarity over the tax planning landscape remains - the “line in the sand” – clearer guidance is needed to avoid HMRC causing greater uncertainty by apparently random pronouncements.

2. The lack of any clearance mechanism for taxpayers without a Customer Relationship Manager (“CRM”) – how do they achieve certainty?

3. Confusion is created of the role of CRMs in clearances – to maintain their credibility, and business certainty, a greater pragmatism is needed.

4. Lack of information on the Advisory Panel composition and role – much more development work needed before its role as a safeguard can be established or confirmed; areas such as roles, governance and independence of interest.

Discussion of these is in detail below, as general comments or in answer to specific questions, with suggestions on how the concerns may be addressed.
1. The “line in the sand” and the tax planning landscape

It is disappointing that the consultation document sidesteps the need for more clarity for taxpayers in general. We note that on paragraph 5.16 of the consultation document that HMRC consider that its CRMs can comment on what is not tax avoidance (the absence of which might suggest something might be). Yet neither Parliament nor HMRC have determined or published a definition of tax avoidance. We repeat therefore, in the interests of certainty for all taxpayers, that it would be our strong preference that that line should be specified. What will be challenged and what will not be should be set out in law after a full consultation process. We consider it is not the function of HMRC, rather that of Parliament, to make the primary decisions on such matters.

An example illustrates the point. The focus of the general anti-abuse rule is supposed to be artificial and abusive tax arrangements, through the legislative definitions of an “abusive” arrangement, as set out in section 3 of this consultation document. In particular, at 3.15 it is stated that the GAAR will be available to alter tax consequences that “manifestly would not have been countenanced by Parliament, had it foreseen the arrangements and the claimed tax consequences”. At 3.17 it is established that “the taxpayer or HMRC may wish to rely on published material from an authoritative text indication how a particular arrangement is normally structured (so as to compare it with the actual arrangement).” This is further expanded at 4.7 in relation to evidence that may be taken into account by a court or tribunal, as including “material in the public domain and evidence of published practice at that time”.

This gives the clear impression that a tax planning route relying on legislative wording that is long established, published and well understood in terms of practical application, even if perhaps not fully as Parliament may have intended (or without particular clarity as to that intention), will not be caught by the general anti-abuse rule. Parliament could have corrected the drafting if it wished at any time with a specific provision; the absence of which is how published practice becomes established.

Consider then the legislation in part 14 CTA 2010. It has been recognised for many years, as being effective only if a particular ordering of steps occurs in relation to the change of ownership of a company and a major change in the nature or conduct of its trade. A brief foray into the ICAS library reveals, in a widely read and respected book (even in the 6th edition, published in 1994), “Taxation of Companies at Company Reconstructions”, by Bramwell, Hardwick, James and Kingstone, full details of the provision and when the loss restriction does and does not apply, according to the ordering of events. One might therefore have considered arranging a company’s affairs so as to protect trading losses in such circumstances was in accordance with published practice at that time, and that Parliament had been accepting of the drafting, whether or not it was its original intention. It is unlikely that many tax professionals would regard this as tax avoidance, never mind aggressive or abusive planning.

However, the HMRC consultation document, “Lifting the Lid on Tax Avoidance Schemes” in relation to the disclosure regime, uses a different conceptual term, “benign” tax planning, as discussed at 5.33. The first example given at 5.33 then causes concerns about the intention of these proposals and the landscape of tax certainty. It describes “arrangements which go beyond what could reasonably be described as benign planning; for example, involving the acquisition by a group of a trading company with carried-forward losses, followed by the transfer of the trade to another company in the group after which the trade undergoes a major change in its nature and conduct…”. This is exactly the situation that might have been concluded on not to have been caught by the GAAR as explained above, nor to be challengeable tax avoidance, but the publication of this statement puts clearly into the tax practitioner world an indication that HMRC may challenge its use, understood to be a change in practice over many years. This causes uncertainty and serves to illustrate the point being made on the need for greater clarity from HMRC.
There may be challenges in defining in legislative terms where, as we would call it “the line in the sand” is drawn, but if these consultations are to be meaningful and effective, and avoid creating more uncertainty in the tax landscape, greater clarity on the intended coverage of the various anti-avoidance measures are needed.

2. **Clearance mechanisms for those without a Customer Relationship Manager**

We accept the concern about the resource implications for clearances on this issue, but in the uncertain landscape described above, and where the Advisory Panel safeguards and guidance are underdeveloped, we consider a mechanism is required to achieve clarity and certainty for taxpayers who do not have a CRM, and to put them on a level of fair treatment with taxpayers who do have a CRM. An alternative discussed might be to use the CAP 1 (replacing COP 10) process at least for an initial period of time and until the ways in which the legislation will be applied has become clearer, or until the published guidance of the Advisory Panel is available to give greater information to allow more secure decisions on likely application to be made. We also consider that for commercial transactions, such as those where existing tax clearance mechanisms have operated for a number of years, it should be taken as a practical outcome that the GAAR would not be invoked in relation to transactions where those clearances have been given. We cannot see how a transaction would fall foul of a GAAR but be within the clearance mechanisms, so wonder why this is such an issue for HMRC?

We also consider the CAP 1 engagement should be regarded as a positive route by HMRC, as it may gain useful information on possible taxpayer behaviours, as well as outcomes and advantages, without the procedural burden of the Disclosure of Tax Avoidance Schemes regime.

3. **The role of the Customer Relationship Manager**

It is only large businesses and certain high net worth individuals who have access to a CRM at present, with whom agreements might be reached as to tax planning that might be regarded as tax avoidance, acceptable or effective as appropriate, or otherwise. We have already commented above on the role of the CRM as described in paragraph 5.16 as commenting on what is not tax avoidance. It is not credible that in this new GAAR environment CRMs could both rule out matters which are not tax avoidance, whilst it “will not provide a formal or informal clearance that the GAAR does not apply”. For the CRM model to deliver value to both sides it is important that comfort can be given in such discussions, to the benefit of both parties, and indeed this is what is understood to be the pragmatic role undertaken with HMRC specialists at present. It would be understandable if HMRC were to put conditions around such clearance, such as the level of openness of discussion and key facts, but otherwise it should indicate why this is not a backward step in delivering certainty to those with a CRM. The CRM model is considered to be a successful one so it would be perplexing indeed, never mind counterproductive, to lessen the value it delivers.

4. **Lack of clarity on Advisory Panel composition and operation**

We are disappointed therefore that the procedural requirements – including details of the legislative protection through the operations of the Advisory Panel - are not being consulted on alongside the core legislation; they are an essential to enable any evaluation of the impact and effectiveness of the overall proposals.

The Advisory Panel proposal is a new development in the UK tax system and is the key safeguard to the GAAR proposals. The draft legislation so far does not even describe or establish the panel. Whilst future details are to be released, this core gap undermines the principle of effective and timely consultation on key tax developments and questions whether this is actually effective consultation on the GAAR proposals in line with government’s stated policy.
Comments on specific consultation document questions

**Question 1**

It would be preferable to have one workable provision establishing the principle in UK tax law, rather than piecemeal adoption or variation, from a simplicity and clarity perspective. We consider it is likely to be in procedural areas such as counteraction (see our response to Question 5 below) and assessment (see our response to Question 10 below) that implementation considerations may arise.

**Question 2**

This would appear appropriate provided the intention of the agreement is not negated.

**Question 3**

The “main purpose” test is accepted given the additional provisions of clause 2 “abusiveness requirement”. Whilst we note the reasons given for omitting the exclusion for arrangements with no tax intent, this should be retained in order to give certainty, for the reasons set out above. The example of concern is where a tax analysis of a genuine commercial transaction takes place and an unexpected tax advantage emerges. The question of fact of a “main purpose” could be more pragmatically resolved by this route.

**Question 4**

The “double reasonableness test” depends, obviously enough, on whose definition of “reasonable” is used, and that embeds a certain subjectivity into the provisions. What is “reasonable” to an experienced tax planner might be more generous than “reasonable” to an activist or campaigner. Whether it operates as intended depends on the way in which it is applied and by whom. In this regard the issues above on certainty, and government and HMRC commitments, are relevant. Assuming these matters are addressed, the approach is appropriate, but we would urge a detailed formal review of the effectiveness of this provision is scheduled after 2 years of operation, to assess this on the experiences gained.

**Question 5**

In the absence of the procedural requirements being made available, and which seems to be a key part to the counteraction, it is rather surprising to see the question posed as it is. We are satisfied with the use of “just and reasonable”. However urgent consideration needs to be given to the appeals process, or process for the agreement of any counteraction, particularly as the types of transaction that potentially would be affected here are likely to be more complex ones in terms of taxpayers, intermediates and commercial steps.

**Question 6**

Counteraction assessments should be subject to time limits, and the taxpayer should be granted the right to make revised claims and elections for not just the year or period in which the counteracting assessment is made, but tax years in which consequential adjustments are made. At present such revision and extension rights are included in provisions such as in section 43A Taxes Management Act 1970.

We note that the consequential adjustment provision is most likely to be relieving, but could increase or create a tax charge. There are natural concerns about the consequences of a counteraction that might apply to a third party who may not be fully aware of the avoidance arrangement or involved in any of the decisions as to the particular structure of a transaction or transactions undertaken by another taxpayer. Such a taxpayer should be protected from any increased tax charge which could unfairly affect their tax position, and it should follow that no interest or penalty exposure should apply to them.
A third party (even an associated one) is unlikely to have full information on the arrangements of the first taxpayer, and so will be unable to consider whether the counteraction or consequential assessment on them was just and reasonable. The obligation is that HMRC “must” make consequential adjustments raises the question as to how this happens given HMRC’s taxpayer confidentiality restrictions.

Procedural details will be required for consequential, as for counteraction, adjustments, and around any appeals procedure.

Whilst there is a preference that any counteraction appeal should be based on the appeals system for an assessment under the appropriate tax as much as possible, it may be that the involvement of different taxes will bring in different sets of rules, particularly if adjustments are required to tax year based assessments, such as capital gains tax, as well as event based assessments, such as an inheritance tax or stamp duty land tax charge. Whilst these occasions may be less common, there should therefore be an overriding principle that such interactions should be dealt with under the GAAR collectively, with the aim that one set of discussions leads to one overall principle, achieving an overall “just and reasonable” outcome and more straightforward process.

**Question 7**

The comments below assume that there is sufficient time in the consultation process for full consideration to be given to the missing details at present, and the guidance in particular. We have serious concerns that the Advisory Panel will not be in place in sufficient time to approve such guidance before the implementation date of April 2013 proposed in the consultation document. In principle, the effective date should be when the GAAR package is ready and not before.

If it is to be implemented as a policy decision regardless, to be consistent with our response to Question 1, adopting one effective date for the provisions of 1 April 2013 would achieve clarity and consistency across taxes. The date would presumably be 6 April 2013 for personal taxes to coincide with the tax year of assessment. This would mean that the mechanism could come into play, in respect of the tax year ended 5 April 2014, assuming that the mechanism builds on existing assessment procedures. Any earlier date than April 2013 will run the serious risk that guidance and procedures will be not be ready anyway, even before taking account of the issues around lack of development at this stage of proposals around the Advisory Panel, procedures or guidance.

The question then is whether there should be transitional provisions for taxpayers undertaking such schemes who have not completed them by 1 April 2013? That would arguably be their own responsibility or misfortune, but on the other hand if it meant that arrangements wholly completed by the effective date would not be caught by GAAR provisions, concerns arise about a “fire sale” behavioural effect.

We are aware how widely trailed the principle of the legislation has been, from the policy announcement in June 2010, through the public dissemination of the report by Graham Aaronson’s study group. If it is also to be addressing only the most abusive and artificial schemes, then they will be running the risk of challenge through the courts anyway and should now be aware of the policy issues around the introduction of a GAAR. Retrospective taxation is something ICAS does not in general support, and so concerns over retrospection arise where arrangements are affected where they are partly completed by 1 April 2013, or any other effective date chosen.

Concerns over a lack of certainty and safeguards have also been raised above. On the basis that these can be addressed, and as a simple solution would be preferable, to exclude from the provisions those not completed by 1 April 2013 but partly entered into before the issue of the final draft guidance approved by the Advisory Panel, assuming it is before that date.
Question 8

No comments; the draft wording is agreed.

Question 9

Agreed; assuming the issues raised above in relation to the Advisory Panel are resolved.

Depending on the effective date adopted, and transitional rules, a different approach may be necessary for arrangements entered into in part prior to the effective date or at an early stage of implementation. The practical case is that consideration would be given to materials in subsection (3) in considering advice to a client on a tax planning arrangement, and it would seem inappropriate that new criterion, such as those in (2) should be applied to such situation retrospectively. For arrangements entered into after the effective date, the provisions proposed appear reasonable; taxpayers will be in a position to make an informed decision on what is relevant.

Question 10

It seems initially rather anomalous to consider a GAAR as applying on a self-assessment basis, as it is difficult to envisage a taxpayer entering into an aggressive tax planning arrangement and not following the hoped for outcome in the tax return filing. This does however give the opportunity for disclosure of planning arrangements entered into, as at present.

Whilst there is a simplicity in using existing legislative assessment mechanisms, concerns arise in relation to permitting other adjustments to be made to tax claims and elections arising from the resulting position, as described in answers to Questions 5 and 6 above.

This is understood to have the practical effect that enquiry windows for, say, income tax self-assessment tax returns would then operate as for enquiries opened under existing provisions.

Question 11

We agree that there should be no penalties applied to any adjustments made, particularly in the early years where the applicability of the regime does not benefit from any issued guidance from the Advisory Panel and if the uncertainty issues above have not been resolved. It should remain the case that a taxpayer taking appropriate professional advice and making appropriate disclosure on a tax return should avoid a penalty and this should be stated in guidance.

Question 12

It would be appropriate and consistent with other legislative provisions to set clear time limits for any Advisory Panel process, but this needs to be considered from an operational perspective. It is HMRC’s proposal to consider the GAAR in line with other enquiries (paragraph 3.35), so HMRC is likely to continue its practice of extensive fact finding and documentary review, whether considering a challenge under a TAAR, case law or a GAAR. This can be time consuming for HMRC and taxpayers, and the enquiry process may invoke formal review or special dispute resolution processes. Procedurally, it is not clear when in this a referral to an Advisory Panel would occur (Stage One), whether a first step for HMRC or a last step in a challenge of a transaction. Correspondingly, a response from a taxpayer (Stage 2) may be prepared as part of an overall response to that enquiry, or be handled separately.

Although the Advisory Panel ruling will not be binding, the practical effect of the “must take into account” provisions in clause 5(2) may mean that taxpayers and HMRC will wish to present full evidence and best case arguments, to any Advisory Panel for a written view. The taxpayer should be permitted time to do this properly but without timewasting. In practice, 30 days will be too short for stage 2; 60 days might be a better target. The same time limit should apply for stage 3. Time limits for stage 4 depend on the administrative arrangements and resources established for the Advisory Panel and what is appropriate. This will also have to be considered in light of assessment time limits.
We consider however that, it should be open to either party to seek an early reference (in terms of ongoing challenge under, for example, case law or a TAAR) to the Advisory Panel, who should be required to answer – yes, no, neutral or not enough information, as set out in paragraph 6.16 within a fixed period; ideally 30 days but no more than 60 days.

Other possible consequences follow the Advisory Panel process being non-binding. Firstly, it might then be up to the taxpayer not to provide the information just for consideration by the Advisory Panel but await any judicial challenge and process, so consideration has to be given to what powers are appropriate for an optional process. Whilst it was proposed that the Advisory Panel would act as a safeguard for taxpayers, and so arguably little benefit would be gained from that approach, that assumes the Advisory Panel will be able to give a ruling, or do so in the taxpayers favour. The possible behavioural responses need to be addressed in further deliberations.

**Question 13**

At a minimum we would expect that, in order for the Advisory Panel to have credibility and play its role in supporting the proper operation of the GAAR within the overall tax system, it should:

1) Comprise a majority of independent members, including an independent chair. Members should have direct experience of the business tax environment; the consequence of the foundation of the legislation on the “reasonableness” test is that the Advisory Panel assessment should be made by those with that appropriate background.

2) Appoint independent members of a similar standing and tax experience to First Tier Tribunal members; that model might provide a useful starting point.

3) Be remunerated on a similar basis to First Tier Tribunal members. It should be established whether First Tier Tribunal members would be eligible to be Advisory Panel members, or be conflicted due to their tribunal role.

4) Be clear on roles and responsibilities; the concern is that HMRC members might represent HMRC’s views, rather than be impartial, due to their employment law duty of care.

Care needs to be taken to ensure that the appropriate legislation passed to bring in provisions that specifically permit confidential taxpayer information to be shared with and considered by the Advisory Panel, who are not employees of HMRC. Care should also be taken to ensure that any taxpayer whose affairs are considered by the Advisory Panel has an opportunity to comment on any proposed publication of decisions reached, in order to maintain anonymity.

**Question 14**

As a key development in UK tax law, it is both appropriate and essential that clarity on the operation of the law is provided on a clear and timely basis. Guidance needs to be provided by the time the draft legislation is published, this autumn and updated on a regular basis, probably twice a year but dependent on activity levels and issues considered. We have commented above on the timing challenges of the initial guidance in relation to effective date time pressures.

We would welcome inclusion of the particular matters described, along with comments to address the concerns on lack of certainty in the provisions, as described above. The composition and resource decisions in relation to the Advisory Panel will be extremely important in the credibility and reliability of this guidance.

The guidance needs also to include details on process, powers and consequential penalties.

**Question 15**

It is not clear how it is possible to observe that a negligible number of small firms will be affected.