TAXREP 38/13

(ICAEW REP 107/13)

ICAEW TAX REPRESENTATION

STRENGTHENING THE CODE OF PRACTICE ON TAXATION OF BANKS

Comments submitted on 15 August 2013 by ICAEW Tax Faculty in response to HM Revenue & Customs consultation document *Strengthening the code of practice on taxation of banks* published on 31 May 2013

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INTRODUCTION

1. ICAEW welcomes the opportunity to comment on the consultation document *Strengthening the code of practice on taxation of banks* https://www.gov.uk/government/consultations/strengthening-the-code-of-practice-on-taxation-for-banks (the code) published by HM Revenue & Customs (HMRC) on 31 May 2013.

2. We should be happy to discuss any aspect of our comments and to take part in all further consultations on this area.

3. Information about the Tax Faculty and ICAEW is given below. We have also set out, in Appendix 1, the Tax Faculty's Ten Tenets for a Better Tax System by which we benchmark proposals to change the tax system.

WHO WE ARE

4. ICAEW is a professional membership organisation, supporting over 140,000 chartered accountants around the world. Through our technical knowledge, skills and expertise, we provide insight and leadership to the global accountancy and finance profession.

5. Our members provide financial knowledge and guidance based on the highest professional, technical and ethical standards. We develop and support individuals, organisations and communities to help them achieve long-term, sustainable economic value.

6. The Tax Faculty is the voice of tax within ICAEW and is a leading authority on taxation. Internationally recognised as a source of expertise, the faculty is responsible for submissions to tax authorities on behalf of ICAEW as a whole. It also provides a range of tax services, including TAXline, a monthly journal sent to more than 8,000 members, a weekly newswire and a referral scheme.

MAJOR POINTS

7. We appreciate the policy purpose behind the Government's proposals and support reasonable and properly targeted measures to address tax avoidance. However, the proposed changes to the operation of the code are fundamentally flawed and potentially damaging to the UK's reputation as a place for inward investment. The proposals need to be reconsidered to ensure that they are proportionate, fair, workable and do not damage the UK's reputation.

8. We are very concerned that while this will remain a voluntary code, banks can be 'named and shamed' for not complying with it following a unilateral decision made by HMRC without any checks and balances other than being reviewed by the Tax Assurance Commissioner, an HMRC appointee. We believe that this is wrong in principle given that naming a bank could potentially destroy its business.

9. The code started life (in 2010) primarily as a way of HMRC being able to more accurately risk assess the banks and work out where HMRC should focus resources. That was a sensible administrative approach and one that introduced an element of self-restraint from the banks.

10. The proposed changes now mean we have the worst of all worlds, an ostensibly voluntary code with great scope for HMRC to act as judge and jury and able to apply a potentially penal legal sanction for non-compliance. If these proposals are to work they need the support of the tax profession and the wider business and banking community. As currently drafted we do not think that this will be the case.

11. We are concerned about the effect of the proposals on the UK's international reputation as a place to invest. The Government is rightly pursuing a growth agenda and seeking to send a clear message that the UK is 'open for business'. As part of that message, it is essential that the UK demonstrates that it is committed to the rule of law. These proposals call into question that commitment.

12. While the current proposal does require the Tax Assurance Commissioner to take the final decision (paragraph 3.5 of the consultation document), this decision will have such fundamental reputational and commercial consequences for the bank in question that it is absolutely essential that there is a formal right of appeal against any decision.

13. The code of practice itself requires the banks, under Section 3 Tax Planning, to reasonably believe that their structures or arrangements are not contrary to the intentions of Parliament or, to reasonably believe, that the proper amounts of tax and national insurance have been paid on the rewards of employment. Given that it is not always clear, for example, what are the intentions of Parliament, we do not believe it is appropriate to require HMRC to be both judge and jury as to whether the bank can be held to have had such reasonable belief.

14. It is therefore essential for there to be independent scrutiny to determine whether or not the bank in question had sufficient grounds for its reasonable belief. It also needs to be remembered that naming and shaming a bank could inflict significant reputational damage for HMRC and its staff, and it would only need one mistake to destroy its credibility with the banking and business sectors as well as leave HMRC vulnerable to legal challenge. If for no other reason we would have thought HMRC would want the protection afforded by an independent review to a Tribunal.

15. Prior to any naming and shaming HMRC should also consult with the Prudential Regulatory Authority and Financial Conduct Authority, as there could be circumstances in which such an action could undermine the stability of the bank in question or even the broader financial system.

16. We note that the new regime for the General Anti-Abuse Rule (GAAR) has established an Advisory Panel to form an independent view on the double reasonableness test. Under that test the GAAR can only apply when the "arrangements cannot reasonably be regarded as reasonable course of action .." We accept that the GAAR imposes a double reasonableness test and the Banking code of practice has only a single reasonableness test. However, in our view it needs to be demonstrated that it was, or was not, reasonable for the bank in question to act as it did and there needs to be a robust, independent, process around that judgement.

17. We presume that the current proposals will not breach the provisions of Commissioners for Revenue and Customs Act 2005 (CRCA) and in particular section 18 in relation to confidentiality. We would welcome confirmation that these proposals will comply with the terms of the CRCA.

18. For the above reasons we do not think that the case has been made for banks to be named and shamed and do not think the Government should proceed with the proposals. If this is meant to be a truly voluntary code then it might be more reasonable, for example, for HMRC to publish a list of banks that have signed up to it and appear to be abiding by its terms.

19. It would then be up to the regulators, the market and wider society to question why a particular bank is not on the list. At that stage we would also expect internal governance and external peer pressure to exert influence on the bank concerned so as to ensure that the bank's activities fell into line with the code.

20. If the Government is determined to proceed with the naming and shaming proposals then as a minimum the banks that HMRC wishes to name should have the right to appeal to an independent panel.

RESPONSES TO CONSULTATION QUESTIONS

Q.1 We welcome respondents' views on whether requiring smaller banks to only adopt Section 1 of the Code remains a tenable approach under the strengthened Code?

21. We do not think the Government has made a case for extending sections 2 to 4 of the Code to smaller banks when it was not deemed appropriate in 2009.

Q2. Views are welcomed from respondents on the proposed timetable for adoption/re-adoption.

22. To allow more time for consultation we think it would be more appropriate for the publication of the list of banks who have confirmed adoption or re-adoption to be put back from Autumn Statement 2013, as proposed in the consultation document, to Budget 2014.

Q.3. HMRC welcomes comments and views on the proposed approach set out to revise the Governance Protocol on Code compliance and whether the proposals provide the necessary assurance safeguards around the naming of non-compliant banks.

23. In our view there must be some process, independent of HMRC, before any bank is named in the annual report, as proposed in the consultation document. We have set out in more detail our views in the Major Points section above.

Q.4. Do these proposals offer sufficient transparency for the public around how the rules will operate?

24. We do not think so. There is already an extraordinary febrile atmosphere in the public domain about tax and large business. Unless the government is prepared to commit to a significant public campaign around the issues raised by the code of practice on taxation for banks then the current proposals are more likely to add to the confusion than resolve it.

Q.5. We also welcome views on whether any other enhancements should be considered at this time to the Governance Protocol.

25. If HMRC is thinking of naming a bank then that bank needs to have formal rights to "engage" in the HMRC process and put forward its own point of view. If a bank is to be named in the annual report then there also needs to be some mechanism such that the bank can present, in the annual report, its own point of view if it believes that it has been named unfairly.

Q.6. We would welcome views from respondents on whether the examples set out below provide a sufficient degree of guidance of the types of transactions, or patterns of transactions or other behaviours that would lead to HMRC concluding that a bank is not complying with its Code commitments?

26. The code of practice in broad terms requires a bank to reasonably believe it is complying with the intentions of Parliament. Many of the examples reach the conclusion that there has been a breach of the code of practice because HMRC believes there has been without an attempt to consider whether the view taken by the bank is reasonable. If HMRC and the bank disagree that is not, of itself, a breach of the code of practice.

Q.7. Do respondents consider this to be an appropriate descriptor for transactions within the ambit of the GAAR?

27. We think the trigger point should be when the Advisory Panel has reached its, independent, opinion that the GAAR should apply.

Q.8. Do respondents agree that this definition will result in appropriate coverage by the Code?

28. We have no comments on this.

Q.9. Do respondents agree that the legislation as drafted covers the issues set out in this Consultation Document appropriately?

29. We have highlighted above some major concerns with the current proposals. These need to be addressed before we can make any comments on the detailed legislation.

Q.10. Are there any other matters that respondents would like to see covered in the legislation?

30. None other than those covered in our comments above.

Q.11. HMRC would also be grateful for any detailed drafting points that respondents might have on the draft clauses.

31. We believe it would be more appropriate to make such detailed drafting points when the more fundamental concerns that we have with the current proposals we have set out above have been addressed.

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APPENDIX 1

ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.

2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.

3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.

4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.

5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.

6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.

7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.

8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.

9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.

10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see icaew.com/en/technical/tax/tax-faculty/~/media/Files/Technical/Tax/Tax%20news/TaxGuides/TAXGUIDE-4-99-Towards-a-Better-tax-system.ashx)