TAXREP 56/15 (ICAEW REPRESENTATION 146/15)

STRENGTHENING SANCTIONS FOR TAX AVOIDANCE

ICAEW welcomes the opportunity to comment on the consultation document *Strengthening sanctions for tax avoidance* published by HM Revenue & Customs on 22 July 2015.

This response of 13 October 2015 has been prepared on behalf of ICAEW by the Tax Faculty. Internationally recognised as a source of expertise, the Faculty is a leading authority on taxation. It is responsible for making submissions to tax authorities on behalf of ICAEW and does this with support from over 130 volunteers, many of whom are well-known names in the tax world. Appendix 1 sets out the ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark proposals for changes to the tax system.

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

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ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.

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General comments

1. The government published an earlier consultation at the end of January 2015 to which we responded TAXREP 24/15 Strengthening sanctions for tax avoidance, in March 2015.

2. In the main our general view has not changed since that earlier response and so we reproduce below the General Comments we made in response to that earlier consultation.

General comments from earlier Representation – TAXREP 24/15

"We understand the public concern about aggressive tax avoidance and support the Government's efforts to tackle aggressive tax avoidance through the use of properly targeted legislation. We note the very considerable number of measures that have been put in place in recent years to clamp down on practices which the Government considers to be unacceptable. The Government's actions in this area were most recently set out in Reducing tax evasion and tax avoidance which was updated on 28 February 2015.

The current consultation sets out proposals for additional sanctions to target persistent tax avoiders who repeatedly use aggressive avoidance schemes in order to defer, reduce, or eliminate, tax liabilities. It is also suggested in the foreword that the time is right to consider an increase in the deterrent effect of the General Anti-Abuse Rule (GAAR) through the introduction of specific GAAR penalties. Our view is that this latter proposal is wholly premature when, as yet, not a single case has even been referred to the GAAR Panel: more time ought to be given to the new, and untested, FA 2013 and NICA 2014 GAAR regime before considering changes.

It is also worth remembering that the GAAR regime was only introduced after a long period of consultation. Graham Aaronson QC established a study group in late 2010 and reported its findings to Government in November 2011. At that stage the proposal was to introduce a General anti-avoidance rule. Following a period of further consultation, led by the Government, provisions were enacted in FA 2013.

We are concerned by the suggestion that the Government might seek to enhance such a recently introduced regime by the introduction of specific GAAR penalties. The GAAR regime has only been in existence for 18 months and the first tax returns, covering the period to 5 April 2014, would only have been lodged by the end of January 2015. Patrick Mears, the Chair of the Advisory Panel, reported in a press interview1in February 2015 that they had so far not looked at any cases and there were none in the pipeline as far as he was aware. It would, therefore, seem to be unreasonably premature to start tinkering with a new system before any cases exist or reliable statistics have become available that would enable that system's impact to be assessed on any reasonable basis.

We are concerned that adding a penalty regime at such an early stage when the GAAR currently remains untested is not necessary. The proposal suggests that the GAAR is considered to be ineffective, when the truth is we do not know on the evidence so far that this is the case. Indeed one measure of success of such a provision is that it does not have to be invoked because taxpayers change their behaviours. Put another way, its prime purpose is to act as a deterrent rather than be used. While we understand the need to address public concerns, we think it should be given time to bed down and an analysis made of its role in curbing unreasonable tax avoidance before any decisions are taken about whether its scope should be extended."

RESPONSES TO SPECIFIC QUESTIONS

How the serial avoiders scheme would work

Q1. Do you agree with a regime based on this model? If not, please outline the reasons for your view.

3. The current proposals target persons who enter into avoidance schemes which fail. There does not seem to be any definition put forward as to what would be considered to an avoidance scheme and in our earlier response we did set out in paragraph 12 our attempt to provide some clarity as to what might be considered to be an avoidance scheme for the purpose of a potential serial avoiders' scheme.

> "We therefore suggest that, to keep the deterrent simple, a serial avoider should be defined as any taxpayer who uses, more than once in a tax year or in any three (or perhaps five) tax years in succession, DOTAS-registered schemes of any kind and also only such schemes which have been found not to work. We believe that would be a fair and objective test which would allow HMRC to apply 'special measures'"

Q2. What do you consider would be a suitable length for a warning period?

4. If the government is going to introduce such a scheme then we accept that any warning period would have to be for a reasonably extended period to make any practical sense.

Sanctions and definitions

Q3. Would requiring serial avoiders to certify annually that they have not employed avoidance schemes, or to provide details of those they have used help discourage further avoidance?

5. This again poses the question as to what is, or is not, an avoidance scheme.

Q4. Which of these approaches would best meet the five penalty principles?

6. We would favour the simple low level of charge.

Q5. If you believe the surcharge should be set at a high level, what should the taxpayer have to do to earn any reduction in the surcharge?

7. Not applicable in the light of the answer to Q4

Q6. What other key features should form part of the surcharge to ensure it meets the five principles?

8. No comment.

Q7. How should a reasonable excuse safeguard be structured to be fair to the taxpayer without undermining the effectiveness of the surcharge? Would excluding advice addressed to third parties, or not made by reference to the taxpayer's circumstances, achieve this aim?

9. We can see the merit of requiring someone who has sought advice on the likely success of a particular arrangement to be required to have received that advice by reference to, and in the context of, their own particular set of facts and circumstances.

Q8. If appealing against the surcharge on the grounds of having taken reasonable care, do you agree that putting the onus of proof on the taxpayer to demonstrate reasonable care would remove any incentive to engage in delaying tactics?

10. We can see the merit of putting the onus on the taxpayer to demonstrate that they have taken reasonable care.

Q9. Do you agree that public naming of the most persistent users of tax avoidance schemes which HMRC defeats would be a fair and effective deterrent? How many schemes should be defeated before it is possible to name a serial avoider?

11. In the light of the extremely serious consequences for the person who is named we agree that there should be safeguards and the power should only be capable of being used in the most egregious of circumstances.

Q10. Do you agree that this would provide sufficient safeguards for naming serial avoiders? If not, what further safeguards do you suggest?

12. We are not at the moment sure that there should not be some right of appeal to an independent person or body rather than depending on actions solely from HMRC.

Q11. Which of these options would provide the best approach to restricting access to reliefs when they have been exploited by a serial avoider as part of a defeated avoidance scheme?

13. The whole purpose of reliefs is to allow, and encourage, taxpayers to take advantage of them. Sometimes when too many taxpayers do take advantage the cost of the relief becomes a concern to the government and the relief is curtailed or abandoned altogether. That does not mean the taxpayer has behaved improperly. The take-up of the relief has exceeded expectations and the cost to the public finances is deemed to be no longer commensurate with the benefit that is likely to be achieved by the relief.

14. We would want to see a robust system in place before the proposal of restricting reliefs was pursued.

Q12. If you favour restricting the power to restrict reliefs to certain categories, how should those categories be defined?

15. No comments at this stage.

Q13. Would focussing on a definition based on schemes notified or notifiable under DOTAS and VADR be sufficient to deter potential serial avoiders from entering into multiple schemes? If not, what other approach do you favour?

16. We think that any serial avoiders' scheme should be based on the existing arrangements for notification of schemes to HMRC.

Q14. Should arrangements to which Follower Notice or GAAR have been applied be included in the definition of a scheme for these purposes? If not, please explain why you do not think this would be appropriate.

17. As in our answer to Q13 we do believe that the existing disclosure arrangements ought to be used.

Q15. Should a scheme be viewed as 'defeated' once a dispute is settled in HMRC's favour, either by agreement with the taxpayer (or, as the case may be, acceptance of a Follower

Notice or GAAR counteraction), or by final litigation being settled in HMRC's favour? If not, what criteria would you apply?

18. We can see the merit in the proposition that when final litigation is settled in HMRC's favour that may be a clear, independent, indication that the scheme has been defeated. But sometimes disputes are agreed by HMRC and the taxpayer because it is deemed by the taxpayer not to be worthwhile pursuing the matter before the Court or because the taxpayer no longer has the funds to do so. We appreciate that HMRC will not "settle" otherwise than in accordance with the Litigation and Settlement Strategy but taxpayers may not pursue particular arguments on the basis of cost or other considerations, not just merely on the merits of the technical argument.

Q16. How do you think a transitional provision should best work to encourage avoiders to withdraw from avoidance schemes they have already employed?

19. We are very much against any new provision which could be seen to have retrospective effect. For that reason we would favour a transition period during which "avoiders could withdraw from schemes (and pay tax accordingly) in order for them to avoid being a potential trigger."

GAAR Penalty Models and next steps

20. For reasons set out in the General Comments above we are not convinced that it is appropriate to introduce penalties under GAAR and so we have not made any comments in relation to the specific questions in the consultation document which we have merely reproduced below.

Q17. Do you agree that the proposed opportunity for taxpayers to correct their tax position is appropriate? Please explain your view.

Q18. Do you agree that the proposed rate for the GAAR Penalty is appropriate? If not, what penalty rate would you propose and why?

Q19. Do you agree that this penalty model will act as a fair and proportionate deterrent? Please explain your view.

Q20. Do you agree that this safeguard would be appropriate for the GAAR Penalty?
Q21. Do you have any views on the development of these measures?

Q22. Would including the definitions listed above as triggering this threshold condition be sufficient? If not, what other approach do you favour?

Q23. What are your views on the options for the trigger for the threshold condition? Please explain your reasoning.

Q24. At what point should a scheme that has high numbers of users count as having been defeated?

Q25. What are your views on the proposed methods of counting defeated schemes that will trigger this threshold condition? Do you think that a rule regarding proportions of cases defeated would be appropriate?

Q26. Do you agree that a period of up to 9 years provides sufficient time to accurately establish regularity of behaviour for this threshold condition? What are your views on the furthest date in the past the authorised officer should consider?

Q27. What provisions should be made for cases that are already in the courts but have not yet concluded?

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 via http://www.icaew.com/en/about-icaew/what-we-do/technical-releases/tax).