



ICAEW TAX REPRESENTATION

HIGH RISK TAX AVOIDANCE SCHEMES

Comments submitted in August 2011 by the Tax Faculty of the Institute of Chartered Accountants in England & Wales (ICAEW) to HM Revenue & Customs in response to the Consultation on High Risk Tax Avoidance Schemes issued on 31 May 2011

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HIGH RISK TAX AVOIDANCE SCHEMES

INTRODUCTION

1. We set out below our response to the Consultation on High Risk Tax Avoidance Schemes published by HM Revenue & Customs on 31 May 2011.

WHO WE ARE

2. The ICAEW operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the ICAEW provides leadership and practical support to over 136,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The ICAEW is a founding member of the Global Accounting Alliance with over 775,000 members worldwide. The Tax Faculty is the focus for tax within ICAEW.
3. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. The Institute ensures these skills are constantly developed, recognised and valued.
4. The Tax Faculty is the focus for tax within the Institute. It is responsible for technical tax submissions on behalf of the Institute as a whole and it also provides various tax services including the monthly newsletter TAXline to more than 11,000 members of the Institute who pay an additional subscription, and a free weekly newswire.

GENERAL REMARKS

5. We fully support the Government's strategy to prevent abuse of the tax system. We have stated consistently that the proper approach to addressing avoidance should be through properly targeted anti avoidance legislation. We also believe that the scope for egregious tax planning would be reduced if the UK tax system was simplified and that the number of changes made year on year was reduced.
6. We believe that the measures that have been put in place over recent years, in particular the Disclosure of Tax Avoidance Schemes (DOTAS) and the changed working relations with large business have made a significant difference to the positive engagement between taxpayers, tax advisers and HMRC. In respect of the former, we have been, and continue to be, fully engaged with HMRC in order to help ensure that the DOTAS rules work as intended while not placing undue burdens on businesses not involved in undertaking such avoidance.
7. The present Consultation looks at ways in which the use of highly artificial schemes can be curtailed or, if not curtailed, made more expensive for their users to remove the cash flow advantage that is gained even when such schemes are unsuccessful.
8. We have a number of concerns about the current proposals.

9. In Chapter 8 it is stated that this is the second stage of the Consultation. This means that Stage 1 'Setting out objectives and identifying options' has already taken place. That stage of consultation was not conducted in the public domain, nor did it involve Representative Bodies such as ICAEW Tax Faculty. We understand that it was conducted with promoters and others involved in schemes which might be caught by the new regime. In the light of concerns about the proper targetting of the new provisions we believe that this consultation should have been undertaken with a much wider group of stakeholders and not just those promoting and using such schemes.
10. Our particular concern is whether this new scheme will add considerably to the existing burdens on business and tax advisers engaged in tax planning which would not appear to fall within schemes that are likely to be listed.
11. We would welcome more evidence as to whether the existing disclosure regime is now sufficiently unsatisfactory that this new additional scheme is required. We believe that HMRC must be more transparent about the extent and nature of the egregious schemes they have uncovered and make a much better case to support the need for this new regime.
12. This should have been Stage 1 of the consultation process and if the DOTAS regime was found to be lacking then Stage 2 could have looked at the best options to supplement that regime.
13. The rationale of this new scheme would appear to be to counter the use of extremely contrived, 'egregious', schemes which HMRC believes are not technically sound but which potentially have the benefit of creating a cash flow advantage for their user.
14. Under current rules, the effect of entering into a scheme which does not achieve its intended purpose is that the tax will have to be paid at some stage, and when it is paid late then there will be an interest charge. The reality therefore is that users of listed schemes will be liable to an additional penalty for using the scheme unless they pay the tax upfront. The penalty would need to be set at a level that deterred taxpayers from using such schemes but at the same time such a penalty would need to satisfy the test of proportionality. Taking a tenable view on the meaning of technically complex legislation (and it should not be forgotten that most of the targeted schemes have the backing of counsel before they are undertaken) is not an offence, civil or criminal. A disproportionate penalty will run a real risk of being struck down by the courts under Article. 6 ECHR (see, e.g. International Transport Roth GmbH [2002] EWCA Civ 158). That is not to say that Parliament should refrain from deterrent measures where there is a real abuse, but the deterrent must be fair.
15. At the same time as this consultation and the preparation of draft clauses is being undertaken, there is a study group under Graham Aaronson preparing a report into the advisability of introducing a General Anti Avoidance Rule (GAAR) in the UK. We have contributed to the work of this group and also held a symposium exploring the advantages and disadvantages of a GAAR. We look forward to contributing further to this work over the coming months and our current understanding is that the Study Group will be seeking to produce a statutory test which will nullify the potential benefit of the most egregious tax avoidance schemes and arrangements. This approach would appear to be broadly along the same lines as this objective and assuming that the group recommend a GAAR there may be merit in considering these proposals as a single package.

DETAILED COMMENTS

Chapter 3 Listing a high risk scheme

Question 1: Do you agree that the taxes listed are the right taxes to include (in the primary legislation providing the power to list a scheme)? Should any taxes be added or deleted from the list, and if so why?

16. We agree that the right taxes have been identified.

Question 2: Do you agree with the proposed criteria for listing a scheme? If not what should the criteria be?

17. There are three criteria listed in paragraph 3.7.

18. The first two would appear to cover very much the same issue i.e. that the person entering into the scheme has done so largely because of the tax benefit that they believe will be the result of so doing.

19. We believe that these two bullet points should be stated as a single criterion.

20. As for the third criterion, which is that HMRC do not believe that the scheme works in the way that it was intended, we agree that HMRC should seek legal advice beforehand. The criterion in paragraph 3.14 is that HMRC has received 'firm legal advice'. We believe that the criterion should be 'unequivocal independent legal advice that the scheme does not work and that it is almost certain that a court would reject the claimed tax treatment'. As a further check, we believe that it ought to require the approval of a senior member of HMRC before a scheme can be listed.

Question 3: Do you consider that the safeguards described are sufficient to ensure that schemes listed are firmly targeted on high risk tax avoidance? If not, what further safeguards would you suggest?

21. The suggested safeguards appear reasonable in ensuring that this scheme is properly targeted and is not applied to schemes that are not high risk.

22. We believe that there should be adequate due process within HMRC itself so and that a senior HMRC official should sign off the case before any listing can take place.

23. As noted above we agree that HMRC should receive independent legal advice from an expert with the necessary experience in these matters. HMRC will need to ensure that the advice is properly independent and that it meets the hurdle set out above, namely that the courts are almost certain to reject the claimed tax treatment.

Question 4: Do you believe that informal consultation would be feasible in the circumstances described? If so, what form might it take and how long would it take?

24. Consultation is one of the fundamental principles of a good tax system. We recognise the difficulty in consulting where tax avoidance is involved and we are not clear at this stage how effective the proposed informal consultation would be. We would be happy to consider this aspect further with HMRC when we have a

clearer idea of the main focus of the scheme and more clarity as to the sort of schemes that are likely to be targeted.

Reporting the use of a listed scheme

Question 5: Do you agree with the proposed time and manner of reporting a listed scheme number?

25. While we can see the merit in the proposals, it is not clear to us the circumstances when a scheme would be listed which has not also required to be disclosed under DOTAS. We believe it would make sense to integrate the two schemes so that they form a coherent and consistent framework for the future (and which takes account of any outcomes from the GAAR study group).

Question 6: Do you agree with the proposed penalty model for failure to report the use of a listed scheme?

26. We can see the merit of a fixed penalty as being simpler to administer but we cannot see why the penalty under the new regime should be greater than the existing penalty under DOTAS. We would also draw attention to the need for a sense of proportion in setting the penalty.

Question 7: Can you suggest ways to avoid requiring a listed scheme user to report both the SRN allocated under DOTAS (if there is one) and the listed scheme number?

27. If the new regime is introduced and a particular scheme has both a DOTAS SRN and is a listed scheme then it would seem most practical for both numbers to be returned.

Question 8: Do you agree that HMRC should inform promoters and users when it is satisfied that a scheme disclosed under DOTAS is a listed scheme? If so, what would be the best way of doing this?

28. It is difficult to answer this question. Given the possible penalty position we believe that HMRC should inform the promoters of such schemes disclosed under DOTAS that they have been listed. This should be done as soon as HMRC has undertaken its due diligence and made a decision to list the scheme.

Payment of the tax in dispute

Question 9: Do you agree with the general principle, described in Chapter 5, governing the design of the additional charge?

29. The principle that underpins the proposed new regime is a matter of concern. We believe that interest on late paid tax compensates the Government for not having received its money at the right time and penalises the taxpayer for having held on to that money longer than they were entitled to. Clearly, this appears to be an insufficient deterrent for some taxpayers on the basis that they will obtain a return on the monies over and above the interest charge. It remains unclear whether the proposed additional charge is actually a penalty or a charge to reflect the fact that the interest charged is not actually a reflection of the true commercial return that could be achieved from withholding the money. In either event, we believe that any charge needs to be proportional. There is also the question as to what happens if the case went to court and HMRC nevertheless lost – would these

amounts be refunded, with interest, possibly at an enhanced rate to reflect the unjust deprivation?

30. We note that in the context of offshore, personal portfolio, bonds and the attempt to discourage their use by UK resident taxpayers an annual compound charge of 15% was introduced in 1999 to discourage their use. That charge is still in place although as part of the Tax Law Rewrite project the provisions are now to be found in sections 515 – 526 ITTOIA 2005. We understand this earlier approach was a success and wonder whether there are any lessons (helpful or unhelpful) that could be learned from it.

Question 10: Do you agree with the model described in Chapter 5 for the additional charge? If yes, to what periods (days, months, quarters etc) should it apply to? If no, please suggest your preferred alternative model.

31. We do not feel able to comment until we are clearer as to what is the real objective of this proposed new regime.

Question 11: What would be the best way to ensure a fair outcome for all individuals who use a listed scheme in circumstances described in Chapter 5?

32. We do not have any proposal to make at this stage.

Taxes Impact Assessment

Question 12: Do you have any comments upon the initial taxes impact assessment?

33. In the absence of any estimate of the Exchequer impact of the proposed measures we have no comment on the current version of the taxes impact assessment.

Further contact

34. For any further enquiries please contact:

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ICAEW AND THE TAX FACULTY: WHO WE ARE

1. ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter which obliges us to work in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 136,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.
2. 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.
3. 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.

THE 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 <http://www.icaew.com/en/technical/tax/tax-faculty/tax-guidance-notes?utm=widget>)